20562

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

APPEAL FROM THE ADMINISTRATIVE LAW COURT

Ralph K. Anderson III, Administrative Law Judge

Case No. 10-ALJ-17-0270-CC

Duke Energy Corporation.....Appellant,

v.

South Carolina Department of Revenue.....Respondent.

RECORD ON APPEAL

VOLUME II

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COPY

SOUTH CAROLINA TAX COMMISSION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

File No. 20090024-9

Duke Power Company — SSN
Name of Taxpayer(s)

P O Box 33189 Charlotte, N.C. 28242
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA TAX COMMISSION consent and agree to the following:

(1) The amount of any STATE Income Tax / License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1983/84 and December 31, 1984/85

may be assessed at any time on or before June 30, 1989
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

Duke Power Co
(Name of Taxpayer)

By: John P. O Neil
(Taxpayer, Partner, Officer of Corp., etc.)

V P, Taxes
(Title)

3/7/89
(Date)

SOUTH CAROLINA TAX COMMISSION

By: Marion M. Lavant pw
(Director, Field Services Division)

3/3/89
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

FS-43 (11/85)

DE00007319

COPY

SOUTH CAROLINA TAX COMMISSION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

File No. 200900249

Duke Power Company — SSN
Name of Taxpayer(s)

Po Box 33189, Charlotte, N.C. 28242
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA TAX COMMISSION consent and agree to the following:

(1) The amount of any STATE Income Tax / License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1983/84, December 31, 1984/85 and December 31, 1985/86 may be assessed at any time on or before December 31, 1989 (Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

Duke Power Co
(Name of Taxpayer)

By: [signature] V.P. Tax
(Taxpayer, Partner, Officer of Corp., etc.)

(Title)

6/19/89
(Date)

SOUTH CAROLINA TAX COMMISSION

By: Marvin N. Durant Rev
(Director, Field Services Division)

5/25/89
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

FS-43 (11/85)

DE00007318

SOUTH CAROLINA TAX COMMISSION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

COPY

File No. 20090024-9

Duke Power Company — SSN
Name of Taxpayer(s)

PO Box 33189, Charlotte, N.C. 28242
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA TAX COMMISSION consent and agree to the following:

(1). The amount of any STATE Income Tax / License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1983/84, December 31, 1984/85, December 31, 1985/86 and December 31, 1986/87 may be assessed at any time on or before December 31, 1990
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

(Name of Taxpayer)

By: John P. O'Neill
(Taxpayer, Partner, Officer of Corp., etc.)

VP Taxes — (Title)

11/8/89 — (Date)

SOUTH CAROLINA TAX COMMISSION

By: Marvin N. Davant Randy Wilson
(Director, Field Services Division)

11/1/89 — (Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

FS-43 (11/85)

DE00007317

SOUTH CAROLINA TAX COMMISSION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

File No. 20090024-9

Duke Power Company SSN
Name of Taxpayer(s)

P O Box 33189, Charlotte, NC 28242 / Attn: Mr. Wilson R. Taylor
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA TAX COMMISSION consent and agree to the following:

(1) The amount of any STATE Income Tax/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1983/84, December 31, 1984/85, December 31, 1985/86, December 31, 1986/87 & December 31, 1987/88 may be assessed at any time on or before December 31, 1991
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

Duke Power Company
(Name of Taxpayer)

By: John H. O. Kelly
(Taxpayer, Partner, Officer of Corp., etc.,)

VA Taxes
(Title)

12/17/90
(Date)

SOUTH CAROLINA TAX COMMISSION

By: Marion N. Dewar / by Ken Regan
(Director, Field Services Division)

December 10, 1990
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

FS-43 (11/85)

SOUTH CAROLINA TAX COMMISSION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

COPY

File No. 20090024-9

Duke Power Company SSN
Name of Taxpayer(s)

P O Box 33189, Charlotte, NC 28242 Attn: Mr. Wilson R. Taylor
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA TAX COMMISSION consent and agree to the following:

(1) The amount of any STATE Income Tax/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1983/84, December 31, 1984/85 December 31, 1985/86, December 31, 1986/87, December 31, 1987/88 & December 31, 1988/89 may be assessed at any time on or before December 31, 1992
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

Duke Power Co
(Name of Taxpayer)

By: [signature]
(Taxpayer, Partner, Officer of Corp., etc.)

V P Taxes
(Title)

12/19/91
(Date)

SOUTH CAROLINA TAX COMMISSION

By: Marvin N. Durant By Randy Wilson
(Director, Field Services Division)

12/13/91
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

FS-43 (11/85)

DE00007284

COPY

STATE OF SOUTH CAROLINA
SOUTH CAROLINA TAX COMMISSION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

FS-43
Rev. (7/90)
2024

File No. 20090024-9

Duke Power Company — SSN
Name of Taxpayer(s)

P O Box 33189 Charlotte, NC 28242 Attn: Mr. Wilson R. Taylor
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA TAX COMMISSION consent and agree to the following:

(1) The amount of any STATE Income/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1983/84, December 31, 1984/85, December 31, 1985/86, December 31, 1986/87, December 31, 1987/88, December 31, 1988/89 and December 31, 1989/90
may be assessed at any time on or before December 31, 1993
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

(Name of Taxpayer)

By: John W. O'Kelley
(Taxpayer, Partner, Officer of Corp., etc.,)

V P Taxes — 12/23/92
(Title) (Date)

SOUTH CAROLINA TAX COMMISSION

By: Marvin N. Davant by Randy Wilson — 12/14/92
(Director, Field Services Division) (Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

DE00007261

COPY

SOUTH CAROLINA TAX COMMISSION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

File No. 20090024-9

Duke Power Company — SSN
Name of Taxpayer(s)

422 South Church Street — Charlotte, NC 28242-0001
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA TAX COMMISSION consent and agree to the following:

(1) The amount of any STATE Corp. Income/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1983/84, December 31, 1984/85, December 31, 1985/86, December 31, 1986/87, December 31, 1987/88, December 31, 1988/89 and December 31, 1989/90 may be assessed at any time on or before December 31, 1994
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

Duke Power Company
(Name of Taxpayer)

By: Robert A. Jolin, VP & Tax Counsel
(Taxpayer, Partner, Officer of Corp., etc.)

V.P. & Tax Counsel — 11-16-93
(Title) (Date)

SOUTH CAROLINA TAX COMMISSION

By: Marvin N. Daward by Randy Wilson — 10/19/93
(Director, Field Services Division) (Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

FS-43 (11/85)

DE00007282

STATE OF SOUTH CAROLINA
DEPARTMENT OF REVENUE AND TAXATION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

COPY

FS-48
Rev. (10/93)
2024

File No. 20090024-9

SSN

Duke Power Company
Name of Taxpayer(s)

422 South Church St. Charlotte, NC 28242-0001
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION consent and agree to the following:

(1) The amount of any STATE Corp. Income/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1983/84, December 31, 1984/85, December 31, 1985/86, December 31, 1986/87, December 31, 1987/88, December 31, 1988/89, December 31, 1989/90 and December 31, 1990/91

may be assessed at any time on or before May 30, 1995
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

Duke Power Company
(Name of Taxpayer)

By: Robert A. Sibley, Vice Pres.
(Taxpayer, Partner, Officer of Corp., etc.,)

Vice President
(Title)

8-29-94
(Date)

SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION

By: Marvin N. Davant Jr.
(Director, Field Services Division)

8/24/94
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

COPY

STATE OF SOUTH CAROLINA
DEPARTMENT OF REVENUE AND TAXATION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

ES-43
Rev. (10/93)
2024

File No. 20090024-9

Duke Power Company — ~~SSN~~ FEI #56-0205520
Name of Taxpayer(s)

422 South Church St. Charlotte, NC 28242-0001
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION consent and agree to the following:

(1) The amount of any STATE Corp. Income/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1983 through December 31, 1990 (Income)
December 31, 1984 through December 31, 1991 (License)

may be assessed at any time on or before November 30, 1995
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

DUKE POWER COMPANY
(Name of Taxpayer)

By: Robert A. Lukens
(Taxpayer, Partner, Officer of Corp., etc.,)

V.P. & TAX COUNSEL
(Title)

5-1-95
(Date)

SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION

By: Joseph P. Southard for Marvin Pevant
(Director, Field Services Division)

2 May 1995
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

DE00007280

STATE OF SOUTH CAROLINA
DEPARTMENT OF REVENUE AND TAXATION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

COPY

FS-43
Rev. (10/93)
2024

File No. 20090024-9

Duke Power Co. SSN FEI# 56-0205520
Name of Taxpayer(s)

422 South Church Street Charlotte, NC 28242-0001
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION consent and agree to the following:

(1) The amount of any STATE Corp. Income/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1983 through December 31, 1991 (Income)
December 31, 1984 through December 31, 1992 (License)

may be assessed at any time on or before June 30,1996
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

Duke Power Company
(Name of Taxpayer)

By: Robert A. Jahn
(Taxpayer, Partner, Officer of Corp., etc.)

V.P. & Tax Counsel
(Title)

8-23-95
(Date)

SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION

By: Marvin A. Davant by RW
(Director, Field Services Division)

8/9/95
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

SOUTH CAROLINA TAX COMMISSION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

COPY

File No. 20090024-9

Duke Power Co. SSN FEI #56-0205520
Name of Taxpayer(s)

422 South Church St. Charlotte, NC 28242-0001
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA TAX COMMISSION consent and agree to the following:

(1) The amount of any STATE Corp. Income/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1978 through December 31, 1992 (Income)
December 31, 1984 through December 31, 1993 (License)

may be assessed at any time on or before June 30, 1997
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

DUKE POWER COMPANY
(Name of Taxpayer)

By: Robert A. Jobson
(Taxpayer, Partner, Officer of Corp., etc.)

V.P.
(Title)

6-3-96
(Date)

SOUTH CAROLINA TAX COMMISSION

By: Marvin A. Daniel RW
(Director, Field Services Division)

5/30/96
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

FS-43 (11/85)

DE00007278

STATE OF SOUTH CAROLINA
DEPARTMENT OF REVENUE AND TAXATION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

COPY

FS-43
Rev. (10/93)
2024

File No. 20090024-9

Duke Power Co. (Now renamed Duke Energy Corporation) SSN FEI #56-0205520
Name of Taxpayer(s)

422 South Church St. Charlotte, NC 28242-0001
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION consent and agree to the following:

(1) The amount of any STATE Corp. Income/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1978 through December 31, 1993 (Income)
December 31, 1984 through December 31, 1994 (License)

may be assessed at any time on or before December 31, 1997
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

Duke Power Co. (Now renamed Duke Energy Corporation)
(Name of Taxpayer)

By: Robert A. Jeffries
(Taxpayer, Partner, Officer of Corp., etc.,)

Vice President and General Counsel-Corporate and Energy Services (Title)

6-25-97 (Date)

SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION

By: Marion H. Davant by Kim
(Director, Field Services Division)

6/20/97 (Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

STATE OF SOUTH CAROLINA
DEPARTMENT OF REVENUE AND TAXATION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

COPY

FS-43
Rev. (10/93)
2024

File No. 20090024-9

Duke Power Co. (Now renamed Duke Energy Corp.) SSN FEI# 56-0205520
Name of Taxpayer(s)

422 South Church St. Charlotte, NC 28242-0001
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION consent and agree to the following:

(1) The amount of any STATE Corp. Income/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended Dec. 31, 1978 through Dec. 31, 1994 (Income)
Dec. 31, 1984 through Dec. 31, 1995 (License)

may be assessed at any time on or before June 30, 1998
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

DUKE POWER CO. (Now renamed Duke Energy Corp.)
(Name of Taxpayer)

By: E. G. Ruff
(Taxpayer, Partner, Officer of Corp., etc.)
Ellen T. Ruff
Vice President and General Counsel, Electric Operations 12/22/97
(Title) (Date)

SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION

By: Marvin N. Leaphart/tb 12/19/97
(Director, Field Services Division) (Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

STATE OF SOUTH CAROLINA
DEPARTMENT OF REVENUE AND TAXATION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

COPY

FS-43
Rev. (10/93)
2024

File No. 20090024-9

Duke Power Co. (Now renamed: Duke Power Corporation) ~~SSN~~ FEI #56-0205520

Name of Taxpayer(s)

422 South Church St. Charlotte, NC 28242-0001

Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION consent and agree to the following:

(1) The amount of any STATE Corp. Income/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1978 through December 31, 1994 (Income)
December 31, 1984 through December 31, 1995 (License)

may be assessed at any time on or before December 31, 1998
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

DUKE POWER CO. (Now renamed Duke Energy Corp.)
(Name of Taxpayer)

By: Cary Flynn
(Taxpayer, Partner, Officer of Corp., etc.,)

Cary Flynn, Vice President Corporate Tax — 6/19/98
(Title) (Date)

SOUTH CAROLINA DEPARTMENT OF REVENUE AND TAXATION

By: Marvin N. Durant by Randy Wilson — 6/15/98
(Director, Field Services Division) (Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

STATE OF SOUTH CAROLINA
DEPARTMENT OF REVENUE

CONSENT TO EXTEND THE TIME TO ASSESS TAX

COPY

FS-43
(Rev. 12/97)
2024

File No. 20090024-9

Duke Power Co. (Now Renamed: Duke Power Corporation) SSN/FEI 56-0205520
Name of Taxpayer(s)

422 South Church St. Charlotte, NC 28242-0001
Address (Number, Street, City or Town, State, ZIP Code)

and the SOUTH CAROLINA DEPARTMENT OF REVENUE consent and agree to the following:

(1) The amount of any STATE Corp. Income/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1978 to December 31, 1995 (Income)
December 31, 1984 to December 31, 1996 (License)
may be assessed at any time on or before December 31, 1998
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-85(C)(5) of the 1976 South Carolina Code of Laws, as amended.

DUKE ENERGY CORPORATION
(formerly Duke Power Co.)
(Name of Taxpayer)

By: Cary Flynn
(Taxpayer, Partner, Officer of Corp., etc.) Cary Flynn

Vice President, Tax
(Title)

(Date)

SOUTH CAROLINA DEPARTMENT OF REVENUE

By: Marcia N. Davant by Randy Wilson
(Administrator, Field Services Division)

12/7/98
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

Original
Mailed
12/22/98
JA

DE00007305

COPY

SOUTH CAROLINA TAX COMMISSION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

File No. 20090024-9

Duke Energy Corp. (Formerly : Duke Power Co.) ~~SSN~~ FEI #56-0205520
Name of Taxpayer(s)

422 S Church St Charlotte, NC 28242-0001
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA TAX COMMISSION consent and agree to the following:

(1) The amount of any STATE Corp. Income/License tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1978 - December 31, 1996 (Income)
December 31, 1984 - December 31, 1997 (License)

may be assessed at any time on or before December 31, 2000
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

Duke Energy Corporation (Formerly Duke Power Company)
(Name of Taxpayer)

By: _____
(Taxpayer, Partner, Officer of Corp., etc.,) C. Flynn

Vice President, Tax
(Title)

December 30, 1999
(Date)

SOUTH CAROLINA TAX COMMISSION

By: Robert K. Anderson
(Director, Field Services Division)

December 17, 1999
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

FS-43 (11/85)

COPY

FS-43
Rev 1/99
2024

State of South Carolina
DEPARTMENT OF REVENUE
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

File No. 20090024-9

Duke Energy Corporation — SSN/FEI 56-0205520
Name of Taxpayer

422 South Church Street, Charlotte, NC 28202-1904
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA DEPARTMENT OF REVENUE consent and agree to the following:

(1) The amount of any STATE Corporate Income/License tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1978 - December 31, 1997 (Income)
December 31, 1984 - December 31, 1998 (License)
may be assessed at anytime on or before December 31, 2001
(Expiration Date)

This agreements extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-85(C)(5) of the 1976 South Carolina Code of Laws, as amended.

Duke Energy Corporation
(Name of Taxpayer)

By: _____
(Taxpayer, Partner, Officer of Corp., etc.)

Senior Vice President Corporate Tax
(Title)

December 15, 2000
(Date)

SOUTH CAROLINA DEPARTMENT OF REVENUE
By: Robert Anderson/ By:

Robert Anderson /BY _____
(Administrator, Field Services Division)

12/15/00
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

State of South Carolina
Department of Revenue
Field Services Division

FS-43

Consent to extend the time to Assess Tax

File#20090024-9
FEI#56-0205520

Duke Energy Corp. (Formerly: Duke Power Co.) & Combined Affiliates
Name of Taxpayer(s)

422 S Church St Charlotte, NC 28242-0001
Address

and the SOUTH CAROLINA DEPARTMENT OF REVENUE consent and agree to the following:

The amount of any STATE Corp. Income/License Fee tax due on any return(s) made by or for the period(s) ended:

December 31, 1978 - December 31, 1997 (Income)

December 31, 1984 - December 31, 1998 (License Fee)

may be assessed at any time on or before December 31, 2001.
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-85(c)(5) of the 1976 South Carolina Code of Laws, as amended.

Duke Energy Corporation
(Name of Taxpayer)

By: _____
(Taxpayer, Partner, Corp.Officer,etc.)

Senior Vice President Corporate Tax
(Title)

12/18/2000
(Date)

SOUTH CAROLINA DEPARTMENT OF REVENUE

By: Robert K. Anderson by TRW
(Director, Field Services Div.)

12/15/00
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer of officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

COPY

State of South Carolina
Department of Revenue
Field Services Division
Consent to extend the time to Assess Tax

FS-43

File#20090024-9
FEI#56-0205520

Duke Energy Corp. (Formerly: Duke Power Co.) & Combined Affiliates
Name of Taxpayer(s)
422 S Church St. Charlotte, NC 28242-0001
Address

and the SOUTH CAROLINA DEPARTMENT OF REVENUE consent and agree to the following:

The amount of any STATE Corp. Income/License Fee tax due on any return(s) made by or for the period(s) ended:

December 31, 1978 - December 31, 1998 (Income)

December 31, 1984 - December 31, 1999 (License Fee)

may be assessed at any time on or before June 30, 2002.
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-85(c)(5) of the 1976 South Carolina Code of Laws, as amended.

Duke Energy Corporation
(Name of Taxpayer)

By: _____
(Taxpayer, Partner, Corp. Officer, etc.)

Senior Vice President Corporate Tax — 12-11-01
(Title) (Date)

SOUTH CAROLINA DEPARTMENT OF REVENUE

By: Robert K. Anderson by TKW — 12/7/01
(Director, Field Services Div.) (Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer of officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

DE00007302

COPY

FS-43
Rev 1/99
2024

State of South Carolina
DEPARTMENT OF REVENUE
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

File No. 20090024-9

Duke Energy Corp.(Formerly Duke Power Co.)&Combined Affiliates SSN/FEI 56-0205520
Name of Taxpayer

422 S. Church St., Charlotte, NC 28242-0001
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA DEPARTMENT OF REVENUE consent and agree to the following:

(1) The amount of any STATE Income/License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1978 - December 31, 1999 (Income) December 31, 1984 - December 31, 2000 (License Fee) may be assessed at anytime on or before December 31, 2002 (Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-85(C)(5) of the 1976 South Carolina Code of Laws, as amended.

Duke Energy Corporation
(Name of Taxpayer)

By: [signature]
(Taxpayer, Partner, Officer of Corp., etc.)

6-21-02
(Date)

Senior Vice President Corporate Tax
(Title)

SOUTH CAROLINA DEPARTMENT OF REVENUE
By: Robert Anderson/ By:

Robert Anderson by [signature]
(Administrator, Field Services Division)

6/21/02
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

Exhibit D

Re-order from Bushnell Company
(215) 842-9520
www.BushnellCo.com

STATE OF SOUTH CAROLINA
ADMINISTRATIVE LAW COURT

Duke Energy Corporation Petitioner, vs. South Carolina Department of Revenue, Respondent.	)	Docket No. 10-ALJ-17-0270-CC **AFFIDAVIT OF MARVIN N. DAVANT**

STATE OF SOUTH CAROLINA)
)
COUNTY OF RICHLAND)

PERSONALLY APPEARED BEFORE ME, Marvin N. Davant, who first being duly sworn, deposes and says as follows:

1. I am over the age of eighteen (18) years old.

2. I was employed by the South Carolina Department of Revenue (formerly known as the South Carolina Tax Commission) (hereinafter referred to as the "Department") for thirty-seven (37) years beginning in 1964 as an auditor with the Estate & Gift Division, an assistant director of the Estate & Gift Division and then the combined Estate & Gift and Income Tax Divisions, and as Director, Field Services Division, until my retirement in 2001. After I retired, I acted as a consultant to the Director of the Department.

3. The Department authorized the Director of its Field Services Division to fill out, execute and issue Form FS-43 to taxpayers.

4. In the performance of my services as Director, I was authorized to issue and execute, and did routinely issue and execute, the Department's Form FS-43, Consent to Extend the Time to Assess Tax.

5. Form FS-43 was a commonly utilized form, to such extent that I, with approval of the Department, allowed my audit deputy to sign the form in the interests of time.

6. It was common practice for the Department to seek an extension of time to make an assessment and request that taxpayer's sign Form FS-43. For example, if auditors were on a short time frame to audit a file, they would request that the taxpayers sign Form FS-43 as an agreement with the Department to extend the time for both assessments and refunds.

7. The Department promulgated and issued Form FS-43 as an official Department form document. To the best of my knowledge, information and belief, the Department has utilized this form since at least the 1960s, as the form was in use prior to the time I became employed with the Department.

8. Form FS-43 was an official form issued by the Department and provided to the Field Services Division for use in its operations.

9. To the best of my knowledge, information and belief, the Department did not issue forms that had not been properly reviewed or approved.

10. The Department's forms identified which division used the form by including the division's name or initial on the form.

11. To the best of my knowledge, information and belief, no individual division of the Department promulgated its own forms, and every form used by any division was an official form provided to it by the Department.

12. The Field Services Division did not review or question Form FS-43 because it was instructed to use the form by the Department.

13. To the best of my knowledge, information and belief, the use of Form FS-43 by the Department was never questioned.

14. To the best of my knowledge, information and belief, the Department historically intended, believed and understood that Form FS-43 not only extended the time to assess additional tax, but also authorized or extended the time for a taxpayer to file a claim for refund within the time stated in the Form FS-43.

15. Prior to enactment of the South Carolina Revenue Procedures Act in 1995, the Department believed that after the execution of the FS-43 by the DOR and the taxpayer that it was authorized and permitted to issue refunds of overpaid tax even if a claim for refund by the taxpayer would not otherwise be timely under the applicable statutory limitations period for filing a refund claim and regardless of whether the period of time initially prescribed for filing a claim for refund had expired.

16. Prior to enactment of the South Carolina Revenue Procedures Act, it was my intent, belief and understanding as Director of Field Services that an executed Form FS-43 constituted the Department's agreement to issue a refund – whether resulting from a review of the taxpayer's records commenced by the Department's on its own initiative, upon consideration of a claim for refund filed by the taxpayer prior to the time stated in the Form FS-43, or otherwise – pursuant to its authority to issue refunds of overpaid tax even if a claim for refund would otherwise be untimely.

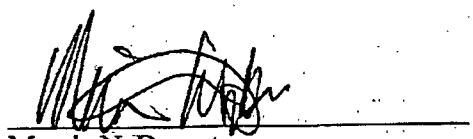
17. After enactment of the South Carolina Revenue Procedures Act, there was no difference in how Form FS-43 was interpreted by Department, and the content of the form remained the same.

18. To the best of my knowledge, information and belief, I had the same authority to sign Form FS-43 before and after enactment of the South Carolina Revenue Procedures Act.

19. Both before and after enactment of the South Carolina Revenue Procedures Act, the purpose of Form FS-43 was to allow the Department and the taxpayer by agreement to extend the time for assessment or refund, whether discovered on audit or a refund claim filed by the taxpayer. The form was specifically used for purposes of recording the agreement to extend the time limitations for both the Department and the taxpayer.

20. It was my intent, belief and understanding as Director of Field Services that a refund claim filed after the statute of limitations had expired would be treated differently than a refund claim filed during the extended period of time agreed to by the Department and the taxpayer by executing Form FS-43. The Department would not consider a refund claim filed in the former situation, but would, in accordance with its agreement, in the latter.

FURTHER AFFIANT SAYETH NOT.



Marvin N. Davant

SWORN and subscribed to before me
this 16th day of May, 2012.

Margie W. Rish (L.S.)
Notary Public for South Carolina
My Commission Expires: 11-4-2020

Exhibit E

STATE OF SOUTH CAROLINA
ADMINISTRATIVE LAW COURT

Duke Energy Corporation Petitioner, vs. South Carolina Department of Revenue, Respondent.	Docket No. 10-ALJ-17-0270-CC **AFFIDAVIT OF ROBERT K. ANDERSON**

STATE OF SOUTH CAROLINA)
)
COUNTY OF RICHLAND)

PERSONALLY APPEARED BEFORE ME, Robert K. Anderson, who first being duly sworn, deposes and says as follows:

1. I am over the age of eighteen (18) years old.

2. I was employed by the South Carolina Department of Revenue (formerly known as the South Carolina Tax Commission) (hereinafter referred to as the "Department") from 1975 until I retired in 2008.

3. While employed with the Department, I served in various positions beginning with an entry-level position with the Audit Division, then was promoted to Regional Manager, then Manager of Audits, then Administrator of Field and Office Operations, and finally was employed as Senior Administrator until the time of my retirement.

4. Since the time I served as Manager of Audits, I had the primary responsibility and authority for executing Form FS-43, Consent to Extend the Time to Assess Tax.

5. In many cases, the authority to issue and execute Form FS-43 was delegated to the auditors auditing a taxpayer's file.

6. Form FS-43 was regularly and commonly used during my employment with the Department, and the Department typically was the party who requested that the form be executed.

7. Form FS-43 is an official document issued by the Department when agreeing to extend the time to assess additional tax or issue a refund with a taxpayer. I do not know when Form FS-43 was first promulgated, but it was many years, if not decades, ago.

8. The use of Form FS-43 was common knowledge within all levels of the Department. To my knowledge, the Department had a process for approving all forms and I assume the Form FS-43 went through such approval process.

9. The Department issued Form FS-43 to obtain the taxpayer's written consent to extend the time to assess or refund additional tax.

10. To encourage a taxpayer's agreement to extend the time to assess additional tax, the Department intended that Form FS-43 similarly extend the time for a taxpayer to file a refund claim with the Department or for the Department to grant a refund.

11. The Department did not issue any other form document or other writing to obtain a taxpayer's consent to extend the statute of limitations.

12. The Department had several revised versions of Form FS-43, all of which were intended to extend the time for the taxpayer to file a claim for refund during the waiver period.

13. By executing Form FS-43, the Department believed that it was exercising its discretionary authority to grant a refund upon examination of a taxpayer's return or otherwise, including the taxpayer's filing a refund claim with the Department within the period of time stated in the FS-43, in exchange for the taxpayer's consent to extend the period of time to assess additional tax.

14. I am not aware of any conflicts or controversy either within the Department or with taxpayers regarding the wording of Form FS-43. To my knowledge, the Department has never refused to honor a valid refund claim filed during the time period covered by Form FS-43.

15. The multiple execution of the Form FS-43s in the Duke Energy Corporation Audits over a long period of years was principally requested by the DOR auditor assigned to the file.

FURTHER AFFIANT SAYETH NOT.

Robert K. Anderson

SWORN and subscribed to before me
this 17th day of May, 2012.

(L.S.)
Notary Public for South Carolina
My Commission Expires: 5/7/22

Exhibit F

Re-order from Bushnell Company
(215) 842-9520
www.BushnellCo.com

RECYCLED PAPER
RECYCLABLE

STATE OF SOUTH CAROLINA

ADMINISTRATIVE LAW COURT

DUKE ENERGY CORPORATION,

Petitioner(s),

vs. Case No: 10-ALJ-17-0270-CC

SOUTH CAROLINA DEPARTMENT OF REVENUE,

Respondent(s).

D E P O S I T I O N

WITNESS: JAN URBAN

DATE: Wednesday, December 21, 2011

TIME: 10:33 a.m.

LOCATION: Willoughby & Hoefer, P.A.
930 Richland Street
Columbia, South Carolina

TAKEN BY: Attorneys for the Petitioner

REPORTED BY: SHERI L. BYERS
Registered Professional Reporter

- -

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A Full-Service Court Reporting Agency
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1-888-988-0086
www.compuscripts.com

may have just seen the attachment.

Q. Was the cover sheet addressed to you?

A. Yes, sir.

Q. And is it sent from Burnie Maybank, Duke's counsel?

A. Correct.

Q. And it was sent on August 12th, 2002, correct?

A. Correct.

Q. And it's entitled Duke Settlement?

A. Correct.

Q. And it states, "Attached is a fax executed copy of the SC870AD sales and use tax. I should have the original to you shortly."

Is that correct?

A. That's correct.

Q. Okay. And you've seen this document before. This is your signature on the bottom of the signed 870AD?

A. Yes, sir.

Q. So it appears from this memorandum that you had sent -- you or Mr. Swearingen, the Department, had sent Duke a form 870AD for sales taxes?

A. That is correct.

Q. And that Duke executed and signed and sent it

back, correct?

A. Correct.

Q. Okay. And to your knowledge, did the Department ever send a similar 870AD for income taxes?

A. Based on the chain of correspondence, it doesn't appear that we would have sent an AD for income taxes.

Q. Is there any reason why you would send one for sales taxes and not for income taxes?

A. It wouldn't -- Duke was requesting an SC870, not an SC870AD. And we -- this was executed in August. The chain of correspondence in which they made clear that they did not want to execute an 870AD was prior to that time, so we apparently did not send them one.

Q. Are you aware of any other document or agreement signed by the Department and Duke Energy that would have prohibited Duke from filing refund claims, in other words, that would have settled their income -- would have prohibited them from filing income tax refund claims? Is there any written settlement agreement between Duke Energy and the Department that you're aware of?

A. I'm not aware of any other written settlement agreement other than the document that you provided that was signed by Mr. Swearingen.

Q. And that document would have held open the periods for Duke to file refunds; is that correct?

A. Would have held open certain periods.

Q. Otherwise open periods?

A. Exactly.

MR. TRESH: Okay. Let's look at 21782.

(PETITIONER'S EXH. 11, Letter Dated December 19, 2002, SCDOR00021782, was marked for identification.)

BY MR. TRESH:

Q. Okay. This is a letter from John Comer to Duke Energy dated December 19, 2002. Do you agree?

A. Correct.

Q. And Mr. Comer was an audit manager for the South Carolina Department of Revenue; is that correct?

A. Yes, sir.

Q. And have you seen this letter before?

A. I don't recall seeing that, no, sir.

Q. Okay. Can you take a moment to look over the letter?

A. Certainly.

Q. Would you agree that this letter was a letter to Mr. Priesmeyer, who was at Duke Energy at the time, and it closed the sales and use tax audit for Duke Energy?

A. Correct.

Exhibit G

RECYCLED PAPER
RECYCLABLE

NEXSEN PRUET
JACOBS POLLARD & ROBINSON, LLC
ATTORNEYS AND COUNSELORS AT LAW

Burnet R. Maybank
MEMBER

DIRECT DIAL:
(803) 253-8228
(843) 720-1768
BMaybank@NPJP.COM

March 20, 2002

Mr. John A. Swearingen
Audit Supervisor
Department of Revenue
301 Gervais Street
Columbia, SC 29201

Jan Steensen Crangle, CPA
Manager, Office of Appeals
South Carolina Department of Revenue
Post Office Box 125
Columbia, SC 29214

Re: Selected Duke State and Local Tax Issues.

Dear John and Jan:

The Duke crowd and I met in Charleston (natch) to discuss the settlement proposals contained in your fax of March 18. We have the following counter-proposal.

First, Duke naturally needs to check your figures. (They had not seen your fax prior to the meeting.) I know there have been issues in the past regarding the calculation of interest, but assuming Duke confirms your figures, we offer the following:

SALES TAX

Duke would like to settle the sales tax liability though 2001, using the methodology and quarterly tax liability contained in your fax. (This has the effect of reducing the amount of our refund.) Duke proposes to execute a SC870AD regarding the sales and use tax liability through 2001.

LICENSE TAXES

Subject to verifying the figures, as stated above, Duke proposes accepting the DOR's proposal and executing a SC870AD for license taxes for the years contained in your proposal. (December 1984 to December 1994.)

INCOME TAXES

Subject to verifying the figures, as stated above, Duke proposes accepting the DOR's proposal except that it would agree to execute a SC870, rather than a SC870AD. This would have the effect of keeping the years open for both the DOR and the State until the end of this year, unless the DOR and Duke jointly agree to execute another waiver.

NPCHAR1:-() -

Duke is examining the possibility of filing amended returns for the purposes of claiming tax incentives, as well as possibly other adjustments. In addition, the files are so stale and the number of years open are so large that Duke is reluctant to close out some 16 years without at least some due diligence, which they have not performed.

CONCLUSION

Duke is actively in the process of verifying the figures contained in your fax, which verification is expected to be completed in the next few days. Please let me know what you think about the other points.

Yours very truly,

Burnet

Burnet R. Maybank

BRM/mwi

cc: Mr. Harley Priesmeyer/Duke Energy

NEXSEN PRUET JACOBS & POLLARD, LLC
ATTORNEYS AND COUNSELORS AT LAW

BURNET R. MAYBANK III
MEMBER

DIRECT DIAL
803-253-8228
BMaybank@NPJP.com

July 2, 2002

Mr. John A. Swearingen
Audit Supervisor
Department of Revenue
301 Gervais Street
Columbia, South Carolina 29201

Jan Steensen Crangle, CPA
Manager, Office of Appeals
South Carolina Department of Revenue
Post Office Box 125
Columbia, South Carolina 29214

Re: Proposed Duke Settlement

Dear John and Jan:

Duke offers the following settlement proposal:

SALES TAX

Duke would like to settle the sales tax liability though 2001, using the methodology and quarterly tax liability contained in your fax. (See attached Exhibit 1.) This includes accepting the DOR's interest rate calculation. Duke proposes to execute a SC870AD regarding the sales and use tax liability through 2001. We understand this equals approximately ($2,796,623) with interest calculated through April 5, 2002.

INCOME AND LICENSE TAXES

Duke proposes accepting the DOR's proposal except that it would agree to execute a SC870, rather than a SC870AD. We understand this would have the effect of keeping the years open for both the DOR and the State until the end of the waiver period (12/31/2002), unless the DOR and Duke jointly agree to execute another waiver. As previously indicated, Duke is examining the possibility of filing amended returns.

We understand that this equals a refund of $5,891,208 (with interest calculated through July 2, 2002.)

We would also like to accept your proposal that the DOR would issue a FAD (at our request) on the calculation of interest on the income and license taxes so that we could contest the interest rate calculations. (Duke may not contest the matter, but we would like to retain the option.)

CONCLUSION

We have pretty well agreed to all of the DOR proposals, so I trust you find this satisfactory. Duke would like to have the attached schedule (Exhibit 2) re-calculated with interest brought forward to no later than July 15th. Additionally, Duke would like for all these matters to be combined for settlement purposes and the DOR issue a refund in a timely manner for the net amount.

If the attached accurately reflects your understanding, please execute a copy of this letter and return it to us. We look forward to receiving the 870 and the 870AD which we will execute and return to you.

With kind regards, I am

Yours very truly,

Burnet R. Maybank III

BRM/kc
cc: Mr. Harley Priesmeyer/Duke Energy

John Swearingen
DOR

July 8, 2002

---- Forwarded by Harley H Priesmeyer/Tax/PSC/PEC on 07/10/2002 11:02 AM

Harley H Priesmeyer
07/09/2002 05:34 PM

To: crangl@sctax.org
cc: bmaybank@npjp.com
Subject: Form SC870

Jan - my lawyers would feel much more comfortable if we can add the following to the instructions on the back of the SC870 form:
"Executing this document does not prevent you from seeking a refund of State taxes paid. The refund claim must be filed within three years from the date the return was filed, (strikethrough: or)two years from the date of payment of the tax or anytime before the expiration of the waiver (12/31/2002), whichever is later.

I think this was the intention of both parties, but I wanted to run this by you before we make this change. Other than this small change, we are prepared to sign the forms and send over to you, probably by tomorrow, if I can find an officer to sign them.

****

Harley Priesmeyer
Director, State and Local Taxes
Duke Energy Corporation
P. O. Box 1642
Houston, Texas 77251-1642

Office: 713-989-3285
Fax: 713-989-3280
Cell: 713-501-0725
email: hhpriesmeyer@duke-energy.com

CC: bmaybank@NPJP.com; SWEARINGEN, JOHN

From: "Harley H Priesmeyer" <hhpriesmeyer@duke-energy.com>
To: <cranglj@sctax.org>
Date: 7/10/02 4:16PM
Subject: Form SC870

Jan - alternatively, we could do without the SC870 for income/license fee if you guys are agreeable to pay us the net amount of approximately $3 million and we get a FAD for the interest calculation. If you are in agreement with this arrangement, let me know and we'll revise the settlement letter.

****

Harley Priesmeyer
Director, State and Local Taxes
Duke Energy Corporation
P. O. Box 1642
Houston, Texas 77251-1642

Office: 713-989-3285
Fax: 713-989-3280
Cell: 713-501-0725
email: hhpriesmeyer@duke-energy.com

---- Forwarded by Harley H Priesmeyer/Tax/PSC/PEC on 07/10/2002 12:04 PM ----

Harley H Priesmeyer
07/10/2002 11:06 AM

To: cranglj@sctax.org
cc: bmaybank@npjp.com
Subject: Form SC870

Jan - I received your voice mail re why we needed to do a SC870 instead of a SCAD870 form. There are two reasons for it. One, Duke wants to reserve the right to contest the interest computation on the income/license fee and secondly, Duke is planning on filing amended returns for some credits and other deductions/adjustments that were previously not taken for these years.

Hopefully, this will aid you re this matter. I remember seeing some previous correspondence from Burney in which you were ok with Duke signing an 870 form.

If you need anything else on this, please let me know.

****

Harley Priesmeyer
Director, State and Local Taxes
Duke Energy Corporation
P. O. Box 1642
Houston, Texas 77251-1642

Office: 713-989-3285
Fax: 713-989-3280
Cell: 713-501-0725
email: hhpriesmeyer@duke-energy.com

---- Forwarded by Harley H Priesmeyer/Tax/PSC/PEC on 07/10/2002 11:02 AM ----

Harley H Priesmeyer
07/09/2002 05:34 PM

To: crangll@sctax.org
cc: bmaybank@npjp.com
Subject: Form SC870

Jan - my lawyers would feel much more comfortable if we can add the following to the instructions on the back of the SC870 form:
"Executing this document does not prevent you from seeking a refund of State taxes paid. The refund claim must be filed within three years from the date the return was filed, (strikethrough: or)two years from the date of payment of the tax or anytime before the expiration of the waiver (12/31/2002), whichever is later.

I think this was the intention of both parties, but I wanted to run this by you before we make this change. Other than this small change, we are prepared to sign the forms and send over to you, probably by tomorrow, if I can find an officer to sign them.

****

Harley Priesmeyer
Director, State and Local Taxes
Duke Energy Corporation
P. O. Box 1642
Houston, Texas 77251-1642

Office: 713-989-3285
Fax: 713-989-3280
Cell: 713-501-0725
email: hhpriesmeyer@duke-energy.com

CC: <bmaybank@npjp.com>

From: JAN CRANGLE
To: URBAN, RON
Date: 7/11/02 11:34AM
Subject: Duke settlement proposal

Would you have some time to discuss this with John and I. The taxpayer is in full agreement with the sales and use tax audit with a balance due of $2.7 million. They want to net this against the refund due on the income and license fee audit, however the tp disagrees with our interest calculations on the income and license audit. The question involves whether simple interest and tax are combined on 9/1/85 (when we adopted compounded interest) and the compounded interest computed on the total. We feel strongly that the DORs administrative practice of compounding only on the outstanding tax balance as of 9/1/85 is proper; however, the taxpayer would like to preserve their right to protest this issue.

The taxpayer also wants preserve their right to file a claim for refund for other deductions and credits. We wanted to close up these years and have them execute an SC870AD so we don't see them again. Since the periods involved date back to 1978 as the result of outstanding IRS RAR adjustments, and most of the early years involve refunds, I want to make sure we are in agreement on how the statute of limitations on refund claims will apply if they don't execute an 870AD.

Thanks.

CC: ANDERSON, ROBERT; COMER, JOHN; SWEARINGEN, JOHN

2/12/02

From: JOHN COMER
To: CRANGLE, JAN
Subject: Duke

Good morning! Any word yet on the 870AD for the sales tax audit? Bill Perry and Carol Solomons are sort of dangling.

I'm also working with Duke on a Special 19 audit for a current construction project. Some of the positions they are suggesting would further widen the strike zone. That makes me a little nervous about the 91-98(01) audit. We really would like to get that one wrapped up. Thanks!

From: JAN CRANGLE
To: COMER, JOHN
Date: 7/12/02 7:40AM
Subject: Re: Duke settlement proposal

It's still in limbo. They are willing to sign the SC870AD on the sales tax, but they don't want to cut the check. I think we'd be OK just having the 870AD executed with the cavet that the payment would be made at the time the income tax matter is resolved. That way it's closed and we are just waiting for payment. What are your thoughts?

>>> JOHN COMER 07/11/02 01:34PM >>>
Jan: Did we get the 870AD signed on the sales tax audit yet, or is it still in limbo depending on the income tax situation?

CC: ANDERSON, ROBERT; SWEARINGEN, JOHN

Exhibit H

RECYCLED PAPER
RECYCLABLE

FS-54

SOUTH CAROLINA DEPARTMENT OF REVENUE
REPORT OF FIELD AUDIT: INCOME TAX & LICENSE FEE

TAXPAYER: DUKE POWER COMPANY
ADDRESS: 422 S. CHURCH ST.
CHARLOTTE, NC 28242-001

FEI # : 56-0205520
FILE # : 20090024-9
PERIOD: 12/78-12/94
DATE: 8/8/02

INTEREST COMPUTED TO: 8/14/02

INCOME TAX:				
PERIOD ENDED:	INCOME TAX	INTEREST	PENALTY	TOTALS
12/78-94	(1,951,189)	(7,434,600)	0	(9,385,789)
LICENSE TAX:				
12/84-94	$835,685	$2,757,796		$3,593,481
SUBTOTAL THRU 3/29/02	-$1,115,504	-$4,676,804	$0	-$5,792,308
UPDATE INTEREST: 3/29 TO 8/14		-$132,889		-$132,889
SUBTOTAL THRU 8/14/02	-$1,115,504	-$4,809,693	$0	-$5,925,197
SALES & USE TAX:				
TAX & INTEREST THRU 4/05/02	$1,725,966	$1,070,657		$2,796,623
UPDATE INTEREST: 4/5-8/14		$60,871		$60,871
SUBTOTAL THRU 8/14/02	$1,725,966	$1,131,528		$2,857,494
INCOME & LICENSE NETTED AGAINST SALES & USE TAX:				-$3,067,703

Exhibit I

STATE OF SOUTH CAROLINA
DEPARTMENT OF REVENUE

OFFER OF WAIVER OF RESTRICTIONS ON ASSESSMENT AND COLLECTION OF ADDITIONAL TAX OR ACCEPTANCE OF OVERASSESSMENT

SC870AD
(Rev. 7/97)
3310

Taxpayer Name(s) Duke Energy Corporation
(Please type or print)

Doing Business As

Street Address PO Box 1642

City Houston State Texas ZIP Code 77251-1642

Identification Number (SSN, FEI, etc.) 56-0205520

Increase (Decrease) in Tax, Interest and Penalties
(Use separate section for each type of tax)

Type of Tax Sales & Use

Period Covered 1/1/1997 through 12/31/2001

Tax $ $1,725,966.09 Penalties $

Type of Tax

Period Covered

Tax $ Penalties $

Total due $ 2,857,494 if paid by August 14, 2002 including interest.

This information was prepared by Ian Steensen Crangle, CPA Telephone Number 803 898.5616

Consent To Assessment and Collection of Additional Tax or Acceptance of Refund Determination

The undersigned consents to the assessment and collection of any additional tax and penalties or accepts any decrease in tax and penalties shown above, plus any interest provided by law. This offer is subject to acceptance by the Department of Revenue. If this offer is accepted, no claim for refund can be filed or pursued and it will not be reopened in the absence of conditions stated in the general information and instructions.

Taxpayer's Signature Date

Spouse's Signature Date

Corporation Name (if applicable) Duke Energy Corporation

By Signature Title Sr. Vice President Date August 13, 2002

Commission Approval of Waiver by

(See reverse side)

JCDC 1600

RECYCLED PAPER
RECYCLABLE

STATE OF SOUTH CAROLINA
DEPARTMENT OF REVENUE

APPLICATION FOR APPEAL

(Protest Pursuant to Revenue Procedures Act)

C-245
(Rev. 1/27/05)
6177

Section I: Taxpayer Identification

Taxpayer Name (s) Duke Energy Corporation (f/k/a Duke Power Company)
(Please type or print)

Address 400 S. Tryon Street, ST22M

City Charlotte State NC Zip Code 28285

Telephone 704/382-1669

Period (s) Covered Periods ending December 31, 1986 to December 31, 1998

Type (s) of Tax (es) Income Tax

Identification Number (Social Security Number, License Number, etc.) 56-0205520

Section II: Department of Revenue Document to be Attached

Please attach a copy of the Department of Revenue document or notice you received which led to the filing of this protest.

Section III: Reason for Protest

State all the reasons you disagree, including a statement of facts supporting your position and the law or other authority upon which you rely. (If the amount of proposed assessment is less than $2,500 you need not provide your legal authority unless you are a partnership, "S" corporation, an exempt organization or an employee plan and the proposed tax is imposed by Chapters 6, 11, or 13 of Title 12.) Add additional sheets if necessary.

See attached.

(over)

Taxpayer's Signature _____ Date _____

Spouse's Signature _____ Date _____

Corporation's Name (if applicable) Duke Energy Corporation

By _____ Title Attorney for the Tax Payers
Signature of Owner/Partner/Officer/LLC Member

_____ Date _____
Print Name

INSTRUCTIONS

The purpose of this form is to reduce to writing those facts and issues with which you disagree. If more space is needed, additional sheets may accompany this form. A protest may be filed by letter rather than using this form; however, all of the information required by this form must be included in the letter and you must comply with the requirements concerning signatures. If you file a joint income tax return, both you and your spouse must sign. If the protest is for a corporation, it must include the corporation's name followed by the signature and title of the corporate officer authorized to sign. If you have any questions concerning this matter, please call the telephone number on the notice or document with which you disagree. Please return document to the Department of Revenue address shown on the notice or document with which you disagree.

Social Security Privacy Act Disclosure

It is mandatory that you provide your social security number on this tax form. 42 U.S.C 405(c)(2)(C)(i) permits a state to use an individual's social security number as means of identification in administration of any tax. SC Regulation 117-201 mandates that any person required to make a return to the SC Department of Revenue shall provide identifying numbers, as prescribed, for securing proper identification. Your social security number is used for identification purposes.

ATTACHMENT TO APPLICATION FOR APPEAL – FORM C-245

Duke Energy Corporation – f/k/a Duke Power Company
File: 20090024-9
Corporate Income Tax
Taxable Periods Ending 12/31/1986 through 12/31/1998

Duke Energy Corporation ("Duke"), formerly known as Duke Power Company files this Application for Appeal in response to the Report of Field Audit ("Report"), dated January 9, 2008 by the South Carolina Department of Revenue ("Department") for the taxable periods ending December 31, 1986 through December 31, 1998 ("Taxable Periods") for corporate income tax. The Duke Tax Department did not receive the Report until February 4, 2008 as evidenced by its date stamp on the attached Report. The Department's Report is attached as Exhibit A.

Facts

Duke is a multistate energy services corporation with operations in South Carolina. In December, 2002, Duke timely filed amended corporate income tax returns for the periods ending December 31, 1986 through December 3, 2001.

The refund claims result from: (a) the filing on a single-factor receipts formula pursuant to South Carolina Code Section 12-6-2290, and (b) the inclusion of gross receipts from the sale of short-term financial instruments in the denominator of its gross receipts factor.

In its original returns, Duke employed the three-factor apportionment formula provided for in Section 12-6-2250. However, the corporation is not among the types of specifically enumerated corporations required to employ the three-factor apportionment formula. Consequently, Duke's amended returns properly employ the single-factor gross receipts formula provided for in Section 12-6-2290.

The amended returns include in the denominator of Duke's single-factor gross receipts formula the corporations' gross receipts from the sale of short-term financial instruments. Duke's day-to-day operations generated excess cash which it desired to keep available as working capital for its business. Consequently, in order to keep the funds as liquid as possible and earn a return, Duke purchased and sold short-term financial instruments. Duke's activities concerning these financial instruments occurred outside of South Carolina. Moreover, the dealer's that assisted Duke with its purchases and sales of the financial instruments were domiciled outside of South Carolina.

In 2007, Duke timely filed amended returns to report changes to its federal taxable income, resulting from the settlement of audit issues with the Internal Revenue Service ("IRS") in December 2006. The changes were reported against the last filed returns filed by Duke, which are currently under appeal with the Department. Those returns claiming refunds for changes to its apportionment factors, as described above, were denied by the

Department and subsequently appealed in March 2003. Such appeals are still pending. The Department ignored the income tax appeals currently pending and adjusted the amended returns filed in 2007 to reflect the apportionment factors on Duke's originally filed income tax returns, not those on its last filed returns.

Reasons for the Appeal

Duke objects to the following determinations of the Department.

1. The Department failed to accept the changes to taxable income resulting from the settlement of federal income tax audits.

2. The Department erred by changing the apportionment factors. Only issues related to the federal income tax changes were subject to change.

3. The Department should have used the apportionment factors from the last filed returns.

4. The denial of Duke's employment of the single-factor gross receipts apportionment formula even though Duke did not satisfy the requirements for using the three-factor apportionment formula under Sections 12-6-2250 or any apportionment formula under Section 12-6-2310.

5. The exclusion of Duke's gross receipts from the sales of the short-term financial instruments from the denominator of Duke's gross receipts factor, notwithstanding that such gross receipts are required to be so included.

6. All other adverse determinations that resulted in the denial of the refund claims.

1. Changes Due to Federal Income Tax Changes

Duke received notices of settlement of numerous changes to its federal taxable income in December 2006. This settlement of issues for the taxable periods was approved by the Joint Committee on Taxation ("Joint Committee") in December 2006. These changes to taxable income were the result of refund claims made while Duke was under audit by the IRS, not by the filing of amended returns with the IRS for which corresponding South Carolina returns were not filed. These changes were not final until approved by the Joint Committee.

2. Change in Apportionment Factors

Duke filed its amended returns for the taxable periods to report the changes to its federal taxable income. It made no changes to the apportionment factors as reported on its last filed returns. As such, the Department is only permitted to audit and make changes to those changes reported by the taxpayer.

3. Last Filed Returns

Duke is required to file amended income tax returns in South Carolina when its taxable income changes due to federal income tax audits. Such changes are required to be made to the last filed returns with the State. Duke filed its amended returns for the applicable tax periods in 2007 using its last filed returns as its starting point. The Department erred in not acknowledging that those returns were still subject to an ongoing appeal and should have postponed any further work on these amended returns until such appeals were exhausted.

4. Single-Factor Gross Receipts Formula

Duke is required to compute its South Carolina corporate income tax liability using a single-factor gross receipts formula to apportion its income. Pursuant to Sections 12-6-2290, if the taxpayer does not derive its principal profits in the manner described in Sections 12-6-2250 or 12-6-2310, the taxpayer must apportion its income utilizing the single-factor gross receipts formula. Duke's business is not among those enumerated in Section 12-6-2310, and it does not satisfy the requirements of Section 12-6-2250. Consequently, Duke is required to compute its South Carolina tax liability using a single-factor gross receipts apportionment formula.

Duke's principal business in South Carolina is not "(a) manufacturing or any form of collecting, buying, or assembling, or processing goods and materials within [South Carolina], or (b) selling, distributing, or dealing in tangible personal property within [South Carolina]." Section 12-6-2250. Duke's principal business in South Carolina was not manufacturing or any form of collecting, buying, assembling or processing goods and materials within South Carolina, as Duke is not a manufacturer, and electricity is neither a good or material. Moreover, Duke was not engaged in selling, distributing or dealing in tangible personal property within South Carolina because electricity is not tangible personal property. See Consolidated Hydro Southeast, Inc. v. South Carolina Dep't of Revenue & Taxation. No. 95-ALJ-17-0634-CC, 1996 WL 909155 (S.C. Admin. Law Judge Div. May 13, 1996) (the sale of electricity constitutes the sale of services and is therefore subject to the additional license fee of Section 12-19-110): Section 12-36-60 (while electricity is included in the sales tax statute discussing the application of the tax on sales of tangible personal property, the sale of electricity is specifically recognized and defined as a service): Section 12-36-910 (subsection A imposes the sales tax on sales of tangible personal property at retail and subsection B imposes the sales tax on sales of various services, including sales of electricity): In re PacifiCorp, 2002-SBE-005-A, 2002 Cal. Tax LEXIS 469 (Cal. S.B.O.E. Sept. 12, 2002), reh'g denied, 2002 Cal. Tax LEXIS 684 (Cal. S.B.O.E. Dec. 19, 2002) (sales of electricity are sales of services and not sales of tangible personal property).

In the letter denying Duke's refund claims, the Department states that its policy on applying the three-factor apportionment formula to power companies as manufacturers should be upheld because it has allegedly been applies for a long period of time. "Such administrative construction however affords no basis for the perpetuation of a patently

erroneous application of the statute." Monroe v. Livingston, 251 S.C. 214,217,161 S.E.2d 243, 244 (1968).

In addition, Duke's filing of amended returns utilizing the single-factor gross receipts apportionment formula does not constitute a change in accounting method that requires the consent of the Department. In the first place, an apportionment formula is not an accounting method. See Section 12-6-4420 (providing that [a] taxpayer's method of accounting. . . must be the same as for federal income tax purposes" and apportionment formulas are not accounting methods for federal income tax purposes).

Moreover, Internal Revenue Service Code Section 446 addresses methods of accounting used in computing taxable income. Under the South Carolina Code, the apportionment methodology is applied after taxable income has been determined. Therefore, the utilization of a statutorily mandated apportionment method after taxable income has been computed is not a change in accounting method as provided in Internal Revenue Code Section 446.

5. Computation of the Gross Receipts Factor

Duke's receipts from the sale of financial instruments are properly included in the denominator of the gross receipts factor for the taxable periods.

First, Duke's receipts from the sale of the financial instruments are business receipts that must be apportioned and not allocated. South Carolina law allocates "[g]ains and losses from the sales of intangible personal property *not connected with the business of the taxpayer* and not held for sale to customers in the regular course of business, less all related expenses" to the corporation's principal place of business. Section 12-6-2250(5) (emphasis added). All items remaining after allocation are apportioned. Section 12-6-2240.

Duke's purchases and sales of financial instruments allow it to maintain its working capital and to increase cash flow for its business. Therefore, the gross receipts from their sale are apportionable. See Eastman Kodak Co. v. South Carolina Tax Comm'n. 308 S.C. 415,418 S.E.2d 542 (1992). The principal used to purchase the financial instruments was generated by Duke's business income, the income produced from the sale of the financial instruments was used in Duke's normal business operations and the instruments were continuously monitored. See M. Lowenstein Corp. v. South Carolina Tax Comm'n. 298 S.C.93, 378 S.E2d 272 (1989).

Second, the gross receipts formula is calculated by dividing a corporation's gross receipts from within South Carolina by the corporation's gross receipts from everywhere. Section 12-6-2290. The source of the gross receipts is the location where the income-producing activity occurs. Lockwood Greene Eng'rs. v. South Carolina Tax Comm'n. 293 S.C. 447,361 S.E.2d 346 (1987). The income producing activity underlying the sale of Duke's financial instruments occurred outside of South Carolina, as all of the corporation's activities regarding the purchases and sales of the financial instruments occurred outside

of South Carolina and the investment dealers that assisted Duke engaged in the buying and selling of the financial instruments outside of South Carolina. Therefore, the gross receipts from the sale of the financial instruments should be included in the denominator, and not the numerator, of the gross receipts formula.

Finally, the denominator of the gross receipts factor includes all receipts from the sale of the financial instruments. The term "gross" is defined, in relevant part, as: "[b]efore or without diminution or deduction. Whole; entire; total; as the gross sum, amount, weight –opposed to net." Black's Law Dictionary 702 (6th ed. 1990) ('Black's"). The term "receipt" is defined, in relevant part as "[t]hat which comes in, in distinction from what is expended, paid out, sent away, and the like." Id at 1260. Given these clear definitions of the controlling language at issue, the amounts received from the sales of the financial instruments constitute gross receipts.

In the alternative, if it is ultimately determined that the three-factor apportionment formula should be used, the gross receipts from the sale of the financial instruments should be included in the denominator, and not the numerator, of Duke's sales factor. Section 12-6-2280(A) provides that the sales factor is comprised of "total sales." Such sales include "sales of intangible personal property and receipts" based on "the entire income-producing activity." Section 12-6-2280(C)(2). As discussed above, all of the income producing activity of Duke's purchases and sales of the financial instruments occurred outside of South Carolina. Therefore, the gross receipts from the sales must be included in the denominator, and not the numerator, of the sales factor.

The amount that should be included in the denominator of Duke's sales factor should be the gross receipts from the sale of the financial instruments. The sales factor includes "total sales." Section 12-6-2280(A). "Total" is defined as "[w]hole, not divided, lacking no part, entire, full, complete, the whole amount." Black's at 1490. Therefore, Duke's gross receipts from its sales of financial instruments should be included in the denominator of the sales factor.

6. General Objection

Duke objects to all other adverse determinations resulting in denial of the refund claims and reserves the right to raise more detailed objections at the conference on this matter.

In addition, Duke objects to the Department's determination on Constitutional grounds. The Department's change to Duke's apportionment factors violates the Due Process and Commerce Clauses of the United States Constitution, as it taxes activity that does not have a substantial nexus with South Carolina, is not fairly apportioned, discriminates against interstate commerce and is not fairly related to the services provided by South Carolina. Moreover, the Department's changes result in a tax due to South Carolina that is distortive, out of all appropriate proportion to Duke's activities in South Carolina and results in the taxation of income by South Carolina that is not properly attributable to South Carolina. E.g., Allied Signal, Inc. v. Director, Div. of Taxation, 504 U.S. 768

(1992); Complete Auto Transit, Inc. v. Brady, 430 US. 274, 279(1977); Hans Rees' Sons v. North Carolina ex. rel. Maxwell, 283 U.S. 123 (1931).

Conclusion

The Department erred by (1) not allowing the changes to taxable income resulting from the settlement of federal income tax audits; (2) changing the apportionment factors on the amended returns; (3) not allowing Duke to employ the single-factor gross receipts formula in computing its corporate income tax liability; (4) not allowing Duke to include the gross receipts from the sale of financial instruments in the denominator of the gross receipts factor; and (5) ignoring the appeals currently pending before the Department, for the same years and for these same issues. The Department has deprived Duke of its constitutional rights.

Duke reserves the right to present further information and raise further arguments concerning its appeal of the Department's audit findings.

Based on the foregoing, Duke respectfully requests a redetermination of the amended returns to reflect the proper federal taxable income, as determined by the Internal Revenue Service, and the proper apportionment factors based on Duke's last filed returns. In the alternative, Duke would request that this redetermination be held in abeyance pending the outcome of the pending appeals.

EXHIBIT A

State of South Carolina
Department of Revenue
301 Gervais Street, P.O. Box 125, Columbia, South Carolina 29214

RECEIVED
FEB 4 2008
CORPORATE
TAX DEPT

January 9, 2008

Duke Power Co.
400 South Tryon St.
Charlotte, NC 28242

Attn: John Lechko
Tax Director

Tax Type	:Corp. Income
Periods	:12-31-86/98
File #	:20090024-9
Response Date	:April 9, 2008
Audit #	:00/36/6361

Gentlemen:

The audit of the above referenced tax return(s) has been completed by the Field Services Division of the South Carolina Department of Revenue. Enclosed is a "Report of Field Audit" (AS-54) which explains our "Proposed Assessment".

If you agree with the changes detailed in the enclosed report, the balance shown to be due on Form AS-54 should be remitted to this office within thirty (30) days from the date of this letter, to avoid additional interest and penalties, if applicable. Please include a copy of the AS-54 with your check to insure proper processing.

If you agree with the Division's adjustments but are unable to make full payment at this time, please complete the enclosed Waiver of Restriction on Assessment (SC 870) and return it to this office within thirty (30) days from the date of this letter. Upon receipt of this document, a "Final Assessment" will be issued.

If you disagree with any of the adjustments of tax, interest, or penalties that have been proposed by the Division, a written protest must be submitted to this office by the response date stated above.

If you do not respond to this letter by the response date stated above, the Division will issue the "Final Assessment" and begin collection action.

Should you have any questions, please do not hesitate to call me at the number listed below.

Yours very truly,

S.C. DEPARTMENT OF REVENUE
LAW & COMPLIANCE

Tim Donovan – Supervisor Non Resident Auditors
(803)898-5619
(803)898-5825 (fax)

/ds
Enclosure

Form Letter AS-54-PA (Rev. 8/95)

SOUTH CAROLINA DEPARTMENT OF REVENUE
REPORT OF FIELD AUDIT: INCOME TAX & LICENSE FEE

TAXPAYER: Duke Power Company
ADDRESS: 400 South Tryon Street
Charlotte, NC 28242

FEI # : 56-0205520
FILE # : 20090024-9
PERIOD: 12/86-12/98
DATE: 1/7/08
AUDITOR: SOUTHARD

INTEREST COMPUTED TO: FEBRUARY 15, 2008

INCOME TAX:

PERIOD ENDED:	INCOME TAX	INTEREST	PENALTY	TOTALS
12/31/86	$0		$0	$0
12/31/87	3,984	15,919	0	19,903
12/31/88	0		0	0
12/31/89	0		0	0
12/31/90	0		0	0
12/31/91	(4,915)	(6,722)	0	(11,637)
12/31/92	0		0	0
12/31/93	0		0	0
12/31/94	(5,647)	(5,663)	0	(11,310)
12/31/95	4,202	5,731	0	9,933
12/31/96	(189,637)	(140,556)	0	(330,193)
12/31/97	(34,780)	(21,685)	0	(56,465)
12/31/98	359,941	298,935	0	658,876
TOTALS	$133,148	$145,959	$0	$279,107

LICENSE FEE:

PERIOD ENDED:	LICENSE FEE	INTEREST	PENALTY	TOTALS
				$0
				0
				0
				0
				0
				0
TOTALS	$0	$0	$0	$0

SUMMARY:	TAX	INTEREST	PENALTY	TOTALS
INCOME TAX	$133,148	$145,959	$0	$279,107
LICENSE FEE	0	0	0	0
TOTALS	$133,148	$145,959	$0	$279,107

SOUTH CAROLINA DEPARTMENT OF REVENUE
RECOMPUTATION OF NET INCOME & TAX

TAXPAYER: Duke Power Company
ADDRESS: 400 South Tryon Street
Charlotte, NC 28242

FEIN: 56-0205520
FILER: 20060024-9
PERIOD: 12/86-12/98
DATE: 1/7/08
AUDITOR: SOUTHARD

PERIOD ENDED:	12/31/1986	12/31/1987	12/31/1988	12/31/1989	12/31/1990	12/31/1991	12/31/1992	12/31/1993	12/31/94	12/31/95	12/31/96	12/31/97	12/31/98
APPORTIONABLE INCOME PER DUKE Settlement of 8/8/02	492,830,271	691,948,173	576,175,037	577,588,551	543,810,293	613,263,092	612,618,376	811,592,332	841,857,719				
APPORTIONABLE INCOME PER ORIGINAL RETURN										1,060,088,378	1,217,711,973		1,294,382,944
APPORTIONABLE INCOME PER AMENDED RET 8/14/07												1,004,268,374	
A ADJUSTMENT 8/14/07	11,685,083	17,818,932	3,726,813	37,117,821	39,272,684	(6,976,828)	(47,038,866)	26,005,931	10,050,795	264,877			
B ADJUSTMENT 8/22/02	(11,685,083)	(17,818,330)	(3,726,813)	(37,117,821)	(39,272,684)	6,662,671	47,038,866	(26,005,931)	(10,050,795)	0	0	0	0
(C)AMENDED RETURN FILED FOR R&D CREDIT & SEC 174	(1,244,938)	(1,993,903)	(7,894,676)	(7,064,660)	(8,562,616)	(6,177,904)	(1,133,387)	(7,215,449)	731,365	(47,933,814)			
(D)AMENDED RETURN FILED FOR R&D CREDIT & SEC 174	1,244,938	1,993,903	7,894,676	7,064,660	8,562,616	6,177,904	1,133,387	7,215,449	(731,365)	47,933,814			
CORRECTED APPORTIONABLE INCOME	492,830,271	692,148,775	576,175,037	577,588,551	543,810,293	612,949,936	612,618,376	811,592,332	841,857,719	1,060,361,255	1,217,711,973	1,004,268,374	1,294,382,944
APPORTIONMENT RATIO-DUKE Settlement 8/8/02	33.9720%	33.2671%	33.4741%	33.4330%	33.1908%	33.6297%	34.0765%	33.4032%	32.5949%		0.000000%	0.000000%	0.000000%
APPORTIONMENT RATIO-ORIGINAL RETURN										31.7270%			
SC PROPORTION	167,495,697	230,267,825	192,858,408	193,104,812	180,483,896	171,997,230	208,724,824	271,191,213	209,212,882	336,417,643	348,876,435	283,917,568	412,870,747
OTHER-SC ALLOCABLE INCOME	16,348	28,158	0	26,483	11,222	84,627	10,881	10,876,721	(389,926)	(489,327)	12,282,211	(17,843,935)	32,136,377
OTHER-SC NOL	0	0	0	0	0	0	0	0	0	0	(569,929)	0	0
TAXABLE INCOME	167,512,345	230,295,981	192,858,408	193,130,875	180,506,121	172,082,107	208,735,686	282,068,934	208,822,957	335,948,316	360,588,717	266,073,633	444,808,124
TAX RATE	5%	5%	5.5%	5%	5%	5%	5%	5%	5%	5%	5%	5%	5%
TAX DUE	8,750,741	13,817,159	10,607,817	9,656,549	9,025,256	8,604,105	10,436,784	14,100,497	10,441,148	16,797,416	18,029,906	13,296,682	22,240,456
TAX CREDIT-Per Original Return	0	0	0	0	0	0	0	0	0	0	(25,000)	0	(693,310)
TAX PREVIOUSLY PAID-ORIGINAL RETURN	0	0	0	0	0	0	0	0	0	(16,793,214)	(18,063,877)	0	(21,257,205)
TAX PREVIOUSLY PAID-AMENDED RETURN 8/14/99	0	0	0	0	0	0	0	0	0	0	0	(13,308,814)	0
TAX PREVIOUSLY PAID-DUKE Settlement 8/8/02	(8,750,741)	(13,813,176)	(10,907,817)	(9,656,549)	(9,025,256)	(8,609,020)	(10,436,784)	(14,100,497)	(10,441,148)	0	0	0	0
UNDERPAYMENT (OVERPAYMENT)	0	3,984	0	0	0	(4,915)	0	0	0	4,202	(78,971)	(7,932)	359,941
TAX PREVIOUSLY PAID (E)	0	0	0	0	0	0	0	0	(5,647)	0	(110,666)	(26,848)	0
INTEREST TO	0	0	0	0	0	0	0	0	0	0	0	0	0
TOTALS	0	3,984	0	0	0	(4,915)	0	0	(5,647)	4,202	(189,637)	(34,780)	359,941

EXPLANATION: TO GIVE EFFECT TO RAR FURNISHED BY TAXPAYER.

A) numbers reflect the RAR amounts for this entity as submitted by taxpayer at 8/14/07.
B) These numbers reflect the RAR amounts for this entity as submitted by taxpayer from the billing of 8/8/02 that combined an income tax refund with a sales tax assessment.
Adjustments A and B are netted as the original RAR from the the 8/8/02 billing is already reflected in the apportionable income of 8/8/02. The tax years 1997 and 1994 result in slight differences in the RAR from 8/8/02 and the RAR from 8/14/07.
C) Taxpayer seems to be taking advantage of amended returns that have been filed with the IRS, but have not been filed with South Carolina and therefore the adjustment would be out of statute.
D) Remove amended return adjustment due to being out of statute.
E) Taxpayer is given credit for the three checks sent to and processed by DOR per enclosed copy of DLN74274838.
The apportionable income numbers above through the 12/94 tax year were determined by the 8/8/02 billing in which the income tax audit refund due was offset by a sales tax audit assessment.
The 12/94 apportionable income is calculated as follows: Original return 831,806,924 plus RAR adjustment on 8/8/02 billing 10,050,795 equals 841,857,719.
The 12/94 return tax paid is calculated as follows: Original return 10,277,346 plus tax amount paid on 8/8/02 billing 163,802 equals 10,441,148.
Taxpayer filed separately with South Carolina through 12/31/95 and combined thereafter.
Please reference Schedules A1,A2 and A3 for the 1996, 1997 and 1998 tax years respectively as these years were filed consolidated.

SOUTH CAROLINA DEPARTMENT OF REVENUE
RECOMPUTATION OF NET INCOME & TAX

Taxpayer: Duke Power Company
Filed: 20080024-8
Period: 12/96-12/96

Schedule: A1
Auditor: SOUTHARD
Date: 1/7/08

Period Ended: 12/96

	Duke Power Company	Crescent Resources	CLT Develop Corp	DE&S	GT&W Gastonia	DukeNet	DE&S Resources	Intera	M-P Supply	Duke Water Systems	Duke Merch	Crescent Comm	Combined
Apportionable Income Per T/P Workpaper:	1,160,104,661	46,151,379	16,329,866	13,605,432	-343,946	-26,327,656	1,272,357	6,575,126	314,776	0	0	0	
Adjustments:													
RAR 5/14/07	-5,123,827	0	0	0	0	0	0	-3,845,840	0	0	0	0	-8,969,667
AMENDED RET FILED FOR R&D CREDIT & SEC 174	20,799,190												
AMENDED RET FILED FOR R&D CREDIT & SEC 174	-20,799,190												
Apportionable Income As Adjusted:	1,154,980,834	46,151,379	16,329,866	13,605,432	-343,946	-26,327,656	1,272,357	1,829,286	314,776	0	0	0	1,206,742,296
Less:Allocable Income Per Original Return	-1,369,716	-49,672,467	-12,746,958	0	71,905	7,595,276	0	0	0	0	0	0	
Total Net Income Subject To Apportionment	1,153,581,119	-3,291,108	3,580,908	13,605,432	-272,041	-17,732,410	1,272,357	1,829,286	314,776	0	0	0	
SC Ratio-Per Original Return b)	30.8249%	45.7257%	4.2226%	7.2963%	28.8401%	36.7039%	4.2482%	0.0000%	0.0000%	0.0000%	0.0000%	0.0000%	
SC Proportion	355,690,226	-1,504,882	151,215	965,687	-66,782	-6,331,091	54,062	0	0	0	0	0	348,875,435
Allocable to SC-Per Original Return	-234,619	12,755,809	-201,848	0	-78,719	21,588	0	0	0	0	0	0	12,262,211
SC Net Income	355,455,607	11,250,927	-50,633	965,687	-145,471	-6,309,503	54,062	0	0	0	0	0	361,167,646
SC NOL	0	0	0	0	0	-296,945	0	0	-272,584	0	0	0	-569,529
SC Taxable Net Income													360,598,117
Tax Rate													0.05
Tax Due													18,029,906
Non-Refundable Credits-Per T/P Workpapers													-396,616
Disallow Non-Refundable Credits a)													396,616
Credits per Original Return													-25,000
Balance													18,004,906
Tax Previously Paid-Per Original Return													-18,083,877
Underpayment(Overpayment)													-78,971

EXPLANATIONS:
a) Taxpayer cannot adjust credits claimed on an original return that was out of statute due to an RAR.

...xpayer cannot adjust any apportionment ratio on an original return that was out of statute due to an RAR. This ratio adjustment refers to Duke Power Company. This ratio for Duke Power Company was adjusted back to the original return. All other ratios from the other entities are in agreement to the original return.

c) Taxpayer seems to be taking advantage of amended returns that have been filed with the IRS, but have not been filed with South Carolina and therefore the adjustment would be out of statute.

d) Remove amended return adjustment due to being out of statute.

SOUTH CAROLINA DEPARTMENT OF REVENUE
RECOMPUTATION OF NET INCOME & TAX

Taxpayer: Duke Power Company
Filed#: 20080024-9
Period: 12/96-12/98

Schedule: A2
Auditor: SOUTHARD
Date: 1/7/08

Period Ended: 12/97

	Duke Power Company	Crescent Resources	CLT Develop Corp	DE&S	GT&W Eastcoast	DukeNet	DE&S Resources	Intera	M-P Supply	Duke Water Systems	Duke Merch	Crescent Comm	Duke Solutions	Combined
Apportionable Income Per Amended Ret 6/4/99:	913,948,040	66,963,676	3,244,584	20,693,063	806,589	-41,093,709	747,010	4,272,362	331,915	0	0	0	-5,031,213	961,683,318
Adjustments:														
RAR 6/14/07	31,892	0	0	-7,106,438	0	0	0	0	938,718	0	0	0	0	-6,135,828
b) AMENDED RET FILED FOR R&D CREDIT & SEC 174	3,745,058													
c) AMENDED RET FILED FOR R&D CREDIT & SEC 174	-3,745,058													
Apportionable Income As Adjusted:	913,980,732	66,963,676	3,244,584	13,587,625	806,589	-41,093,709	747,010	4,272,362	1,270,633	0	0	0	-5,031,213	955,548,256
Less:Allocable Income Amended Ret 6/4/99	2,069,828	0	0	0	-603,841	41,089,071	0	0	0	0	0	0	0	42,555,058
Total Net Income Subject To Apportionment	916,050,560	66,963,676	3,244,584	13,587,625	2,748	-4,638	747,010	4,272,362	1,270,633	0	0	0	-5,031,213	998,103,314
SC Ratio-Per Original Return a)	29.9594%	15.3117%	0.0000%	2.3695%	18.3911%	25.0537%	2.5153%	0.1022%	0.0000%	0.0000%	0.0000%	0.0000%	14.0911%	
SC Proportion	274,462,230	10,252,842	0	321,841	505	-1,162	18,812	4,366	0	0	0	0	-1,131,686	283,917,588
Allocable to SC-Per Amended Ret 6/4/99	-4,409,845	0	0	0	-83,618	-13,459,472	0	0	0	0	0	0	0	-17,949,935
SC Net Income	270,052,384	10,252,842	0	321,841	-83,113	-13,461,634	18,812	4,366	0	0	0	0	-1,131,686	265,973,653
SC NOL	0	0	0	0	0	0	0	0	0	0	0	0	0	0
SC Taxable Net Income														265,973,653
Tax Rate														0.05
Tax Due														13,298,682
Tax Previously Paid-Per Amended Ret 6/4/99														-13,306,614
Underpayment(Overpayment)														-7,932

EXPLANATIONS:
a) Taxpayer cannot adjust any apportionment ratio on an original return that was out of statute due to an RAR. This ratio adjustment refers to Duke Power Company. The ratio for Duke Power Company was adjusted back to the original return. All other ratios from the other entities are in agreement to the original return.

b) Taxpayer seems to be taking advantage of amended returns that have been filed with the IRS, but have not been filed with South Carolina and therefore the adjustment would be out of statute.

c) Remove amended return adjustment due to being out of statute.

SOUTH CAROLINA DEPARTMENT OF REVENUE
RECOMPUTATION OF NET INCOME & TAX

Taxpayer Duke Power Company
Filed: 20000324-0
Period: 12/96-12/96

Schedule: A3
Auditor: SOUTHARD
Date: 1/7/98

Period Ended 1996

	Duke Power Company	Crescent Resources	DLT Develop Corp	PERC	STWW Services	Deltaship	DEBS Management	Intera	M-P Supply	Duke Water Systems	Duke Nomin	Crescent Comm	Duke Solutions	Tropical	DCCMMBR/ Inc	Duke Proj Dev't	Deltaf Mat Inc	Global Asset	Combined
Apportionable Income Per Original Return:	1,276,373,813	58,044,831	3,558,863	-31,171,279	1,363,008	-34,110,724	196,488	-634,103	308,837	0	0	0	-8,272,748	300,045	-697,383	-2,104,279	41,838,158	-48,496,348	17,911,888
Adjustments:																			
PAR 8/14/97	35,997,994	4,369,808	0	189,844	0	0	0	84,929	0	0	0	0	0	0	0	-6,833,898	0	0	
a) AMENDED NET FILED FOR R&D CREDIT & SEC 179	-36,948,846																		
c) AMENDED NET FILED FOR R&D CREDIT & SEC 179	34,948,818																		

...ome As Adjusted:	1,317,371,717	63,414,631	3,558,863	-36,971,735	1,363,008	-34,110,724	196,488	-449,174	308,837	0	0	0	-8,272,748	300,045	-697,383	-10,778,997	41,838,158	-48,496,348	1,311,974,843
...Income Per Original Return	-1,977,357	-49,343,169	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	
Total Net Income Subject To Apportionment	1,315,394,360	14,071,462	3,558,863	-36,971,735	1,363,008	-34,110,724	196,488	-449,174	308,837	0	0	0	-8,272,748	300,045	-697,383	-10,778,997	41,838,158	-48,496,348	
SC Ratio-Per Original Return 4)	99,447%	19.413%	0.000%	0.000%	94.334%	27.749%	11.467%	0.000%	0.000%	0.000%	0.000%	0.000%	1.761%	7.725%	0.247%	0.000%	0.194%	0.000%	
SC Properties	438,373,836	-2,753,329	0	-483,599	196,361	-8,477,866	22,517	0	0	0	0	0	-145,191	23,221	-1,836	-8,433	78,631	-186	443,988,124
Allocate to SC-Per Original Return	441,199	11,317,491	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	33,196,677
SC Net Income	438,813,035	58,843,979	0	-483,599	196,361	-8,477,866	22,517	0	0	0	0	0	-145,191	23,221	-1,836	-8,433	78,631	-186	0
SC NOL	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	644,988,190
SC Taxable Net Income																			0.05
Tax Rate																			32,249,409
Tax Due																			-999,519
Credits per Original Return																			31,647,144
Balance																			-31,647,295
Tax Previously Paid-Per Original Return																			-151
(Underpayment)/Overpayment																			

EXPLANATIONS

c) Taxpayer cannot adjust any amendment ratio on an original return that was out of statute due to an RAR. This ratio adjustment relates to Duke Power Company. The ratio for Duke Power Community was adjusted back to the original return. All other ratios from the other entities are in agreement to the original return.

b) Taxpayer seems to be taking advantage of amended returns that have been filed with the IRS, but have not been filed with South Carolina and therefore the adjustment would be out of statute.

c) Reasons amended return adjustment due to being out of statute.

South Carolina
Department of Revenue
P.O. Box 125, Columbia, SC 29214

CE-2

ST 20M



JOHN LECHKO
TAX DIRECTOR
DUKE POWER CO
400 SOUTH TRYON ST
CHARLOTTE NC 28242

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Exhibit K

RECYCLED PAPER
RECYCLABLE

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Re-order from Bushnell Company
(215) 842-9520
www.BushnellCo.com

RECYCLED PAPER
RECYCLABLE

State of South Carolina
Department of Revenue
301 Gervais Street, P.O. Box 125, Columbia, South Carolina 29214

SC REVENUE PROCEDURAL BULLETIN #00-3

SUBJECT:	Claims for Refund and Correction of Errors in Tax Years Barred by Time Limitations
EFFECTIVE DATE:	Applies to all periods open under the statute.
SUPERSEDES:	SC Revenue Procedure #95-5 Commission Decision #93-1 All other previous documents and any oral directives in conflict herewith.
REFERENCES:	S. C. Code Section 12-60-470 (2000) S. C. Code Section 12-60-2150 (2000) S. C. Code Section 12-54-85 (As Amended August 2000) S. C. Code Section 12-60-40 (2000)
AUTHORITY:	S. C. Code Ann. Section 12-4-320 (2000) S. C. Code Ann. Section 1-23-10(4) (Supp. 1999) SC Revenue Procedure #99-4
SCOPE:	The purpose of a Revenue Procedural Bulletin is to provide procedural guidance to the public and Department personnel. It is a written statement issued to assist in the administration of laws and regulations by providing guidance that may be followed in order to comply with the law. **A Revenue Procedural Bulletin does not have the force or effect of law, and is not binding on the public.** It is, however, binding on agency personnel until superseded or modified by a change in statute, regulation, court decision, or advisory opinion.

INTRODUCTION

The South Carolina Code of Laws sets forth time limits within which the Department of Revenue must assess and collect taxes and within which taxpayers must file claims for refunds. The United States Supreme Court in Rothensies v. Electric Storage Battery Co., 329 U.S. 296 (1946) noted that the "statute of limitation is an almost indispensable element of fairness as well as of practical administration of income tax policy."

The purpose of this advisory opinion is to set forth the Department's authority for granting refunds and briefly describe the remedies provided by law which may be available to taxpayers and the Department, where appropriate, that allow correction of errors that would otherwise be barred by time limitations.

GENERAL RULE FOR CLAIM FOR REFUND - CODE SECTIONS 12-60-470, 12-60-2150, and 12-54-85

Code Section 12-60-470 contains the general rule applicable to claims for refunds of taxes, other than property taxes. The section provides, in part:

> (A) A taxpayer may seek a refund of any state tax by filing a written claim for refund with the department. A claim for refund is timely filed if filed within the period specified in Section 12-54-85 even though the time for filing a protest under Section 12-60-450 has expired and no protest was filed.

Code Section 12-60-2150 contains the general rule applicable to claims for refunds of property taxes administered by the Department. The section provides, in part:

> (A) Subject to the time limitations in Section 12-60-1750[1], and within the time limitation of Section 12-54-85(F), a property taxpayer may seek a refund of property taxes paid and assessed by the department by filing a claim for refund with the department if it originally assessed the property or the taxpayer believes the property is exempt, other than from the homestead exemption, from property taxes.

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[1] Notwithstanding any other provision of law, Code Section 12-60-1750 provides that no refund of property taxes must be given: (1) for a property tax exemption requiring an application, unless the application was timely filed; or (2) for errors in valuation, unless the assessment was appealed in accordance with Section 12-60-2110, 12-60-2510, or 12-60-2910, as appropriate. For purposes of this item, the taxation of exempt property is not an error in valuation.

Code Section 12-54-85, the general statutory rule for filing a claim for refund for all fees and all taxes administered and collected by the Department, provides for the time periods within which to timely file a claim for refund. The section provides, in part:

> (F)(1) Except as provided in subsection (D)[2] above, claims for credit or refund must be filed within three years of the time the timely filed return, including extensions, was filed, or two years from the date of payment, whichever is later. If no return was filed, a claim for refund must be filed within two years from the date of payment.
>
> (2) If the claim was filed by the taxpayer during the three-year period prescribed in item (1), the amount of the credit or refund may not exceed the portion of the tax paid within the period, immediately preceding the filing of the claim, equal to three years plus the period of any extension of time for filing the return.
>
> (3) If the claim was not filed within the three-year period, the amount of the credit or refund may not exceed the portion of the tax paid during the two years immediately preceding the filing of the claim.
>
> (4) If no claim was filed, the credit or refund may not exceed the amount which would be allowable under item (2) or (3), as the case may be, as if a claim were filed on the date the credit or refund is allowed.

[2] Notwithstanding any restrictions on filing a claim for refund provided in subsection (F), subsection (D)(3) allows a person to file a claim for refund resulting from an overpayment due to changes in taxable income made by the Internal Revenue Service within one hundred and eighty days after the date a final determination of tax adjustment (i.e. the federal assessment date) is made by the Internal Revenue Service. The refund described in this subsection applies only to the overpayment of taxes resulting from adjustments of the Internal Revenue Service.

SUSPENSION OF TIME LIMITATIONS FOR CLAIM FOR REFUND OR CREDIT - CODE SECTION 12-60-40

As stated above, Code Section 12-60-470 grants the Department the authority to issue refunds provided such claims are submitted within the time limitations of Code Section 12-54-85. These time limitations, however, may be extended or suspended as authorized by Code Section 12-60-40 which provides:

> (A) A taxpayer may waive his rights under this chapter [Chapter 60 - The South Carolina Revenue Procedures Act], providing the waiver is in writing and is signed by the taxpayer or his representative. The department may extend any time limitations provided by this title and for any other taxes. The department and a taxpayer may agree to extend any time limitations or waive any requirements provided in Article 5 [State Revenue Appeals Procedure] or Article 9 [Property Tax Protest, Appeal, and Refund Procedures] of this chapter.
>
> (B) Time limitations provided under this chapter [Chapter 60 - The South Carolina Revenue Procedures Act] and Chapter 54 [Uniform Method of Collection and Enforcement of Taxes Levied and Assessed by the Department] are suspended during a stay ordered by the Taxpayers Rights Advocate.

See also Code Section 12-54-85(G) which provides for a suspension of the time limitations provided in subsections 12-54-85 (A), (B), (C), (D), and (E) in certain situations, such as for 90 days after the date of a proposed assessment, or during the pendency of a stay ordered by the Taxpayers' Rights Advocate.

CLARIFICATION TO THE GENERAL RULE FOR CLAIM FOR REFUND

As discussed above, Code Section 12-60-470 grants the Department authority to issue a credit or refund for taxes, other than property taxes, provided such claims are submitted within the time limitations provided in Code Section 12-54-85.

Consistent with its longstanding administrative position, the Department will continue to interpret the time limitations in Code Section 12-54-85 consistent with the following rules:

1. If the taxpayer agrees to the Department's request that a waiver of the time limitations on assessments be extended, then the time the Department may mail a notice of assessment pursuant to Code Section 12-54-85 will be extended. In so doing, the Department will also consider the time within which a taxpayer may file a claim for refund to be extended until the agreed upon date, however, if the Department's extension is limited in any way, such as to a particular issue, then the extension for a refund by a taxpayer will be limited in the same way. This position only applies to effective extensions agreed to in writing with the Department.

2. A taxpayer must file a claim for refund within the time limitations and state the reasons for that request. Code Section 12-60-470(B)(5) requires a claim for refund to state the amount claimed, but, if after filing a timely claim for refund, the taxpayer discovers that a refund greater than the amount originally requested is due, the Department will consider such claims, but only if the adjustment is based upon issues raised in the timely filed claim for refund. No additional refund is allowed for new issues raised after the time limitations has expired.

3. Setoff, the doctrine of equitable recoupment, or the mitigation provisions provided in Internal Revenue Code Sections 1311 - 1314 apply to the situation, as briefly described below.

In the Department's opinion it does **not** otherwise have the authority to allow correction of errors that are barred by the time limitations for any reason, including situations where:

1. A mistake is made calculating the expiration date of the time limitations.

2. A taxpayer failed to file a timely claim for refund when another state assessed a tax on the same income taxed in South Carolina. A taxpayer in a situation where it is undetermined which state is due the tax should file a protective claim with the Department within the time limitations. See item 2 above.

Code Section 12-60-470(G) provides that:

> Even if a taxpayer has not filed a claim for refund, if the department determines that money has been erroneously or illegally collected from a taxpayer or other person, the department, in its discretion, may, upon making a record in writing of its reasons, grant a refund to the taxpayer or other person.

Code Section 12-60-2150(G) similarly provides that:

> Even if a taxpayer has not filed a claim for refund, where no question of fact or law is involved, and it appears from the record that money has been erroneously or illegally collected from a taxpayer or other person under a mistake of fact or law, the department may, subject to the limitations in Section 12-60-1750, within the period specified in Section 12-54-85 and upon making a record in writing of its reasons, order a refund to the taxpayer or other person.

The Department uses Code Section 12-60-470(G)[3] and 12-60-2150(G) when it audits a taxpayer and determines that the taxpayer is entitled to a refund. It has been and is the Department's longstanding administrative opinion that its right to grant a refund to a taxpayer pursuant to this section is limited by time limitations, *i.e.*, that it cannot grant a refund unless at the time the Department grants the refund, the taxpayer could have filed a timely claim for refund. In 1995, the General Assembly enacted Code Section 12-54-85(F)(4) which is consistent with this opinion. In the opinion of the Department, if it refuses to grant a refund pursuant to this section a taxpayer is not entitled to a hearing, and the taxpayer is not entitled to appeal the Department's decision. However, if the taxpayer files a claim for refund before the expiration of the time limitation, the taxpayer is entitled to a hearing and an appeal of the Department's decision.

SUMMARY OF SETOFF, DOCTRINE OF EQUITABLE RECOUPMENT, AND MITIGATION PROVISIONS

SETOFF. In general, setoff permits all items involving the same tax and the same taxable period to be considered for adjustment in determining whether there has been an overpayment or underpayment of tax. Setoff does not permit recovery of an underpayment or overpayment in and of itself, instead it operates to decrease the recovery claimed by the other party.

---

[3]This provision was previously contained in Code Section 12-54-30 which was repealed and replaced by Code Sections 12-60-470(G) and 12-60-2150(G) in 1995. A taxpayer was not entitled to a hearing; there was no appeal granted from an adverse decision; nor was there any reference to a statute of limitations. See Argent Lumber Co. v. Query, 178 SC 1, 182 S.E. 2d 93 (1935) where, in a similarly worded statute, the court determined that "under the terms of this act the tax commission is clothed with the power and authority to make such refunds for valid reasons, but no corresponding right is conferred upon the taxpayer to compel by suit the exercise of this authority; so that if such legislation enacted subsequent to the time of the payment of the taxes now sought to be recovered, should be held applicable, the petitioner has no legal right of redress under the specific terms of this section, for the recovery of taxes paid...."

Setoff may be used by the Department to reduce or eliminate a refund claimed by a taxpayer. For example, a taxpayer files a claim for refund for erroneously paid tax. Although the time limitations on assessments is closed, the Department is permitted to review the return for other errors. Setoff allows the Department to reduce the amount of the taxpayer's claim for refund by the amount of any error, the correction of which would result in additional tax being due. The refund may be reduced to zero, however, the Department may not make an additional assessment.

Setoff is also available as a remedy to taxpayers. For example, a taxpayer under audit is subject to a longer time limitation on assessments under Code Section 12-54-85(C)(1), (2), or (3). The taxpayer discovers an error, the correction of which would result in a refund, for the period under audit. Since the time limitations on claims for refund has expired, the taxpayer cannot obtain a refund. Setoff may be used by the taxpayer to setoff the potential refund amount against the amount of an assessment by the Department. The assessment may be reduced to zero, however, the taxpayer may not receive a refund.

For an interpretation of setoff by the courts see, Lewis v. Reynolds, 284 U.S. 281 (1932).

The following general principles are applicable to the doctrine of setoff:

1. The claim arises from the same tax.

2. The claim arises from the same taxpayer.

3. The claim arises from the same taxable period.

THE DOCTRINE OF EQUITABLE RECOUPMENT. In general, the doctrine of equitable recoupment permits a taxpayer or a taxing authority to make up for a mistake in the tax treatment of a transaction in a closed tax period by adjusting an amount involving the same transaction in an open tax period. The doctrine, however, may only be raised in conjunction with a tax dispute that is not barred by the time limitations. Like setoff, the doctrine of equitable recoupment permits a refund claimed by a taxpayer or an assessment made by the Department to be reduced to zero, and does not permit the taxpayer to receive a refund or allow the Department to make an additional assessment.

The application of the doctrine of equitable recoupment to tax law was analyzed in the following four U. S. Supreme Court decisions: Bull v. United States, 295 U.S. 247 (1935); Stone v. White, 310 U.S. 269 (1937); Rothensies v. Electric Storage Battery, 320 U.S. 296 (1946); and McEachern v. Rose, 302 U.S. 56 (1937).

Bull describes how recoupment applies to a situation involving double taxation (income tax and estate tax) of a single item of income. An estate received income from a partnership following the death of a partner. Estate tax was erroneously paid on the income. After the time limitations on filing a claim for refund for estate taxes had run, the Internal Revenue Service determined that the partnership income was subject to federal income tax. Since the statute was open on the income tax issue, the executor paid the tax, but sued to recoup the barred overpayment of estate taxes. The court ruled that the estate should have been entitled to credit the estate tax overpayment against the income tax deficiency.

In Stone, the Internal Revenue Service used the doctrine of equitable recoupment to recoup a barred deficiency from a refund due to a related person. The trustee paid income tax on trust income. The beneficiary erroneously excluded the trust income from her individual income tax. The IRS erroneously assessed an income tax deficiency against the trust, after the time limitations was closed with respect to the beneficiary. The trustee paid the tax and sued for a refund. The Court ruled that the trustees and the sole beneficiary must be considered as one and allowed the Internal Revenue Service to recoup the deficiency of the beneficiary against the overpayment of the trust.

The following general principles are applicable to the doctrine of equitable recoupment:

1. The taxable event claimed upon and the one considered in recoupment arise from a single item or transaction occurring in different years.

2. The single transaction must be subject to two taxes based upon inconsistent legal theories.

3. The amount claimed in recoupment must be barred by the time limitations while the disputed amount must be timely.

4. If more than one taxpayer is involved, there is an identity of interest between the taxpayers.

5. It applies in situations not covered by the mitigation provisions.

THE MITIGATION PROVISIONS. The mitigation provisions are set forth in Internal Revenue Code Sections 1311 - 1314. South Carolina has adopted these Internal Revenue Code provisions, and the Department will apply them to determinations made under South Carolina income tax laws only, where applicable.

In general, the mitigation provisions permit an error to be corrected even though correction of the error in a closed year is prevented by some provision or rule of law. Unlike setoff and the doctrine of equitable recoupment, the taxpayer may receive a refund under the mitigation provisions, and the Department may make an additional assessment.

Many factors must be present in order for the mitigation provisions to be used to correct an error in a year closed under the time limitations. Some of the factors include:

1. A "determination" for an open period must establish that the same item has been treated erroneously in a prior, closed year. "Determination" is defined in Internal Revenue Code Section 1313 and generally includes a court decision or administrative action.

2. On the date of the determination, the correction of the error in the closed period must be barred by the operation of law, such as the time limitations, or rule of law, such as estoppel or res judicata. Operation of law, however, does not include the mitigation provisions or offers-in-compromise.

3. The determination creates a "circumstance of adjustment" that includes one of the following conditions defined in Internal Revenue Code Section 1312:

   a. Double inclusion of item of gross income,
   b. Double allowance of deduction or credit,
   c. Double exclusion of item of gross income,
   d. Double disallowance of deduction or credit,
   e. Correlative deductions or inclusions for trusts or estates or for legatees, beneficiaries, or heirs,
   f. Correlative deductions and credits for related corporations, or
   g. Basis of property after erroneous treatment of prior transaction in certain circumstances.

If all of the required conditions are met, then the mitigation provisions apply and the error period is reopened for a limited period of time. The adjustment may be made to correct errors that relate to a single item or to an affected item. No other items are reopened. Internal Revenue Code Section 1314 sets forth the rules concerning the amount and method of adjustment.

CONCLUSION

It is the Department's policy to allow claims for refund as provided in Code Sections 12-60-470, 12-54-85, and 12-60-40, and, as provided in this advisory opinion.

Be advised that this advisory opinion is intended to provide only a brief overview of setoff, the doctrine of equitable recoupment and the mitigation provisions. There are numerous court cases and articles available that discuss these three remedies in detail. Questions concerning the specific applicability of setoff, the doctrine of equitable recoupment and the mitigation provisions should be directed to your tax advisor.

SOUTH CAROLINA DEPARTMENT OF REVENUE

s/Elizabeth A. Carpentier
Elizabeth A. Carpentier, Director

December 4, 2000
Columbia, South Carolina

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South Carolina Revenue Ruling No. 87-5, 09/16/1987

Date Issued: 09/16/1987

Tax Type: Corporate Income Tax, Personal Income Tax RR-87-5 TAX CREDIT FOR NEW JOBS

SUPERSEDED BY RR #99-5

REFERENCE

Modified by Code Section 12-7-1220 (formerly (12-7-616), Code of Laws of South Carolina.

QUESTIONS

1. What is the definition of the term "full-time employee" as used in § 12-7-1220?
2. What is the definition of the term "service related industry" as used in § 12-7-1220?

FACTS

Several industries have inquired as to what constitutes a "full-time employee" and what industries are considered "service related industries" as used in the determination of the tax credit for new jobs.

DISCUSSION

Section 12-7-1220(B) as amended provides as follows:

> "Permanent business enterprises engaged in manufacturing, processing, warehousing, wholesaling, research and development, and service related industries in counties designated by the commission as less developed areas are allowed a job tax credit for taxes imposed by § 12-7-230 equal to $1,000 annually for each new full-time employee job ..."

The wording above is repeated in subsections (C) and (D) of § 12-7-1220, except that the amount of the credit differs. There are no definitions within the statute as to the particular meaning of "full-time employee" and "service related industry."

1. Full-time is defined in Webster's dictionary as "the amount of time considered normal or standard for working during a given period." There are numerous definitions and court cases dealing with the number of hours required of a "full-time employee." One of the most widely known appears to be the number of hours required by a full-time employee as used by the Bureau of Labor Statistics. The Bureau of Labor Statistics for employment and unemployment cites a full-time worker as "those employed 35 hours a week or more."
2. The South Carolina Supreme Court (*Fennell v. South Carolina Tax Commission, 103 S.E.2d 424*) cited the following definition of "service" from Webster:

"Any result of useful labor which does not produce a tangible commodity. In economics, such business concerns as railroads, telephone companies or laundries and such persons as physicians, are regarded as performing services."

Thus "service related industries" would be businesses primarily engaged in providing services as opposed to retail businesses engaged in selling merchandise for consumption or manufacturing business engaged in transforming materials or substances into new products.

The determination as to whether a business is a service related industry can be made by comparing the gross receipts of the business derived from providing services to total gross receipts of the business. If over 50 percent of the gross receipts are from providing services, then the business would be service related. This method has been utilized by the commission in determining whether a multistate taxpayer is providing services and thus would utilize the gross receipts ratio to apportion its income. (A multistate taxpayer deriving over 50 percent of its income from dealing in tangible personal property would utilize the three factor ratio to apportion its income).

CONCLUSION

For purposes of determining the tax credit for new jobs the following definitions shall apply.

"Full-time employee" - As a general rule, it shall be presumed that an employee who works at least 35 or more hours per week is a full-time employee. However, if the facts show that a lesser number of hours is standard or customary for a particular job or industry, then a lesser number may be allowed.

A "service related industry" shall mean a business that derives over 50 percent of its gross receipts from providing services (as opposed to selling or dealing in tangible personal property).

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1984 WL 184988 (S.C.Tax.Com.)

Tax Commission
State of South Carolina

*1 RE: INCOME TAX

I-D-352

March 26, 1984

FINDINGS OF FACTS

"X" Company is a utility company incorporated in South Carolina. Pursuant to its business of generating electricity, "X" entered into an agreement with "Y" Corporation in which "Y" agreed to supply uranium to "X" at an agreed upon price. "Y" was unable to comply with the agreement and "X" brought an action for breech of contract.

A subsidiary of "X" was created as "Z" Company. "Z" Company was established for the purpose of financing the acquisition, ownership and carrying of nuclear fuel to be used by "X". "Z" Company finances the purchase of nuclear fuel by issuing commercial paper which is guaranteed by "X". "Z" Company has no employees and all expenses relating to the nuclear fuel are paid by "X". "X" has the use, control and exclusive possession of the nuclear fuel and the "Z" Company provides services only to "X".

"X" assigned to "Z" Company all of their rights in and title to the contract for uranium with "Y". A settlement agreement was reached in which "Y" agreed to compensate "X" for damages by payment. As the result of an audit report, a determination was made that "X" was subject to the license fee on gross receipts under § 12–19–110. This matter came before us as a conference under § 12–1–80 in January 1984.

CONCLUSION

Section 12–19–110 imposes an annual license fee of three mills upon the entire gross receipts from business within this State of a utility company. To be taxable, the statute requires the litigation proceeds to be (1) gross receipts, (2) from business within the state and (3) of a utility company.

Gross receipts is a broad term which includes all proceeds received by the entity so long as such receipts resulted from any part of its business. Sandusky Gas and Electric Co. v. State, 151 N.E. 685. Regulation 117–89.1 does not limit the meaning of gross receipts to receipts from operations; it merely says gross receipts "shall include all receipts from operations", but does not say that such was all that is included. To so read Regulation 117–89.1 would be to ignore the broad language in § 12–19–110 which uses the term "entire gross receipts".

The gross receipts here are from the utility company's business since they arose from a breech of contract to purchase uranium to be used to generate electricity. Further, the receipts were from business done within South Carolina since the uranium was to be used in this State. It should be noted that the proceeds resulted from a suit

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brought within South Carolina, and it is of no consequence that the action was settled in another state after a consolidation of similar suits. It is the nature of the origin of the action which makes the proceeds business receipts and here the origin of the proceeds was a suit to recover damages for uranium purchases required to fulfill "X's" business as a utility.

Finally, we find and conclude that the proceeds from the litigation are that of proceeds of a utility company. There can be no dispute that "X" is a utility company and we find and conclude that even though "Z" Company received actual payment, for tax purposes "X" is the constructive recipient of the proceeds. It is well settled that the substance of a transaction must govern over the form. Beard v. South Carolina Tax Commission, 230 S.C. 357, 95 S.E.2d 628. In the instant case, the facts demonstrate that the "Z" Company is only a corporate shell having no employees of its own and operating only as a financing vehicle for purchasing fuel. All obligations of "Z" Company are guaranteed by "X" and all expenses related to fuel are paid by "X". "Z" Company sells to and buys for "X" only. Further we note "Z" Company was created only after the litigation had begun and that by order of the Public Service Commission, the damages awarded "X" must be used by "X" to reduce the cost of fuel it purchases with such cost reduction passed on to "X's" customers. Because of such we conclude the proceeds are received for tax purposes by "X".

*2 We also note in passing that the only issue before us is the license fee liability under § 12–19–110 of "X" and not that of the corporate shell "Z" Company. However, "X" argues that it is not subject to the tax since the proceeds were actually received by "Z" Company and that "Z" Company is not liable since it is not within § 12–19–110. We disagree. We find that "X" is the constructive recipient; however, if it were not, "Z" Company would be liable. The record shows that "Z" Company is regulated by the Public Service Commission as an affiliate of "X". We find that "Z" Company is such an integral part of "X's" business that it also is a utility. Its sole function is to acquire fuel to enable "X" to generate electricity and is as crucial to the utility as is the transmission of electricity for sale. However, since we find and conclude "X" is liable for this tax and since the liability of "Z" Company is not before us, we present our conclusions as to "Z" Company's liability only for completeness.

AND IT IS SO FOUND AND ORDERED. (March 26, 1984)

Note: Commission Decisions dated before 1987 are from Volume 1 of the South Carolina Tax Commission Decisions. These decisions do not have specific page references, therefore, citations are not available.

1984 WL 184988 (S.C.Tax.Com.)

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Date of Printing: Jun 27, 2011

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RE: INCOME TAX, 1984 WL 184988 (S.C.Tax.Com.) ((Mar 26, 1984))

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1985 WL 192739 (S.C.Tax.Com.)

Tax Commission
State of South Carolina

*1 RE: CORPORATE LICENSE FEE

I-D-384

May 17, 1985

FINDINGS OF FACTS

"X" Company was incorporated as a utility in another state. Shortly thereafter, it qualified to do business in South Carolina.

As part of its operations, "X" owned a power plant located in South Carolina. This property was used by "X" in the production of electricity and is identified as "Y" Station.

"X" sold a percentage of unit 1 of its "Y" Station and a percentage of the plant's suport facilities to the "Z" Electric Cooperative and an out-of-state Electric Membership Cooperative. Included within these transactions were various contractual entitlements and other assets not located in this State.

When the Field Services Division of the South Carolina Tax Commission audited "X", it determned that "X" had failed to include the amount of gross receipts from these sales attributable to the sale of the real property and improvements situated in South Carolina, within its tax base for purposes of computing its corporate license fee liability as required by § 12–19–110. In view of such, the Division proposed an additional license fee assessment against "X" based upon this amount.

"X" has excepted to the Division's proposed assessment and is now before this Commission contesting the same pursuant to § 12–47–440. Its exception is based upon four distinct points.

"X" first argues that South Carolina's corporate license fee on utilities is not imposed upon the receipts received from the sale of assets. Rather, it maintains that the fee is limited to the receipts it receives from customers for the furnishing of electricity.

Secondly, "X" contends that the receipts from the sale of unit 1 and its support facilities are not receipts from business within South Carolina. In making this contention, "X" notes that a majority of such property was sold to an out-of-state purchaser, Electric Membership Cooperative, and that the sale itself was consummated in that state.

Next, "X" states that if the receipts from this sale are subject to South Carolina's corporate license fee, then the amount includable in the tax base should be limited to the net derived therefrom. "X" claims that it netted very little on the transactions.

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Finally, "X" questions the constitutionality of South Carolina's corporate license fee scheme. In doing so, it alleges the § 12–19–110 violates the equal protection clauses of both the United States and South Carolina Constitutions.

CONCLUSION

Chapter 19 of Title 12 of the Code of Laws of South Carolina, 1976, imposes an annual license fee upon certain corporations that are organized under South Carolina law or that are qualified to do busines in South Carolina. The meausre of the fee depends upon the nature of the corporation itself. In the instant situation, § 12–19–110 levies the license fee that gives rise to the issues raised by "X". The relevant portion of that provision states:

*2 "In addition to the license fee provided by § 12–19–100 and any and all other license taxes and fees or taxes of whatever kind, there is hereby levied an annual license fee of three mills upon the entire gross receipts from business within this State during the calendar year next preceding by every ..."

The above language clearly indicates that the license fee on power companies, such as "X", is based on entire gross receipts and not just receipts from customer charges. Where a statute is clear and unambiguous, there is not room for construction and the terms of the statute must be given their literal meaning. Southeastern Fire Ins. Co. v. South Carolina Tax Commission, 253 S.C. 407, 171 S.E.2d 355 (1969) and Green v. Zimmerman, 269 S.C. 535, 238 S.E.2d 323 (1977).

Although "X" argues that the use of the word "operations" in § 12–19–110's original enactment (See Act No. 269, Acts of 1904.) indicates that the subject fee is to be limited to customer charges, we do not give the word such a narrow interpretation. The term "operations" implies more usually relates to the whole process of planning for and operating a business. Liller v. Logsdon, 261 Md. 367, 275 A.2d 469 (1971).

It should also be noted that the Tax Commission has long interpreted § 12–19–110 as applying to more than the mere receipts from customer charges. This interpretation has been promulgated into Tax Regulation 117–89.1 wherein it is stated:

"Gross receipts, as used in § 12–19–110 of the South Carolina Income Tax Act of 1926, as amended, shall include all receipts from operations within the State, and also other profit and loss items with a local situs. Intangible income from intangibles used in the conduct of the business within this State shall be included in gross receipts."

We are likewise of the opinion that the receipts arising from the sale of the subject property are receipts from business in this State. The assets themselves are business assets located in South Carolina. The fact that one of the purchasers was from out-of-state and that the transaction itself was consummated out-of-state does not distract from the local situs of the property. In point of fact, if the situation was reversed and "X" sold similar assets located in the other state to a South Carolina purchaser after consummating the transaction in this State, we would not include the gross receipts derived therefrom in "X's" corporate license fee base.

We are aware of the fact that while the gross receipts from the subject sale were large, "X's" net was minimal. Unfortunately, however, we cannot ignore the language of § 12–19–110. The license fee must be levied upon gross receipts, not net receipts. The two are something separate and apart. "Gross receipts" have been defined to mean the whole receipts as opposed to net receipts. Taylor v. Rosenthal, 308 Ky. 4,213 S.W.2d 435 (1948) and First Trust Co. of St. Paul v. Commonwealth Co., C.C.A.S.D., 98 F.2d 27 (1938).

*3 Further, the fact that Tax Regulation 117–89.1 makes reference to "profit and loss items" does not imply that

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the fee levied by § 12–19–110 is based on net receipts. That language is used to identify certain items and does not relate to the manner of taxation. To interpret 117–89.1 otherwise would ignore the broad language of § 12–19–110. A regulation cannot change the meaning of a statute. Heyward v. South Carolina Tax Commission, 240 S.C. 347, 126 S.E.2d 15 (1962).

Finally, although this Commission does not have the authority to decide the constitutionality of § 12–19–110, we do note that the General Assembly has the power to make reasonable discriminations between various kinds of corporations for tax purposes. Whether such discrimination is reasonable in the instant situation is not for us to decide.

Based upon the foregoing, it is our conclusion that the Field Services Division's audit adjustments should be upheld.

AND IT IS SO FOUND AND ORDERED. (May 17, 1985)

Note: Commission Decisions dated before 1987 are from Volume 1 of the South Carolina Tax Commission Decisions. These decisions do not have specific page references, therefore, citations are not available.

1985 WL 192739 (S.C.Tax.Com.)

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Attorney General Opinion 04/02/2012

Cite(s): Attorney General Opinion 04/02/2012

Issue Date: 04/02/2012

Tax Type(s): Cigarette, Alcohol & Miscellaneous Taxes

OPINION

April 2, 2012

Joshua A. Gruber, Esquire

Office of the County Administrator, Beaufort County

Administration Building

Post Office Drawer 1228

Beaufort, South Carolina 29901-1228

Dear Mr. Gruber:

You have requested an opinion of this Office concerning the proper interpretation of the term "gross income" in the context of a county business license tax ordinance. Specifically, you have asked which "items as reported on a federal income tax return should be included and [which] items should be excluded" when calculating the gross income of a private club or homeowners' association pursuant to Beaufort County's ordinance.

As an initial matter, we note that you have not provided this Office with any information regarding the activities or sources of income of any particular club or association. Thus, we can provide only general guidance, beginning with the presumption that the county's ordinance is valid as written. *See, e.g.,* Letter to The Honorable N.R. "Bob" Salley, Sr., Op. S.C. Att'y Gen. (Nov. 18, 1996). [1]

Analysis

"Gross Income" as defined by ordinance

Beaufort County Code section 18-51 imposes a business "license fee based on gross income." In general, gross income in the context of a business license tax "means the total receipts from a business before deducting expenditures for any purpose." Columbia Ry., Gas & Elec. Co. v. Jones, 119 S.C. 480, 112 S.E. 267, 272 (1922) ; *accord* Letter to The Honorable J. Ira Ruff, Op. S.C. Att'y Gen. No. 83-76Att'y Gen. No. 83-76 (Sept. 26, 1983). For the purposes of its business license tax, Beaufort County appears to use the terms "gross income" and "gross receipts" interchangeably. [2] Section 18-47 of the Beaufort County Code defines "gross receipts" as follows:

> *Gross receipts* means the total revenue of a business, received or accrued, for one calendar or fiscal year collected or to

> be collected by the businesses [sic], excepting income from business done wholly outside of the unincorporated area of the county and fully reported to a municipality or other county. The term "gross receipts" means the value proceeding or accruing from the sale of tangible business personal property, including merchandise and commodities of any kind and character and all receipts, by the reason of any business engaged in, including interest, dividends, discounts, rentals of real estate or royalties, without deduction on the account of the cost of the property sold, the cost of the materials used, labor or service cost, interest paid, or any other expenses whatsoever and without any deductions on account of losses. Gross income for business licenses purposes, [sic] may be verified by inspection of returns filed with the Internal Revenue Service, the South Carolina Department of Revenue, the South Carolina Insurance Commission, or other government agency. In cases of brokers or agents, gross income means commissions received or retained, unless otherwise specified. Gross income for insurance companies means gross premiums collected. Gross income for business license tax purposes shall include the value of bartered goods and/or trade-in merchandise.

This definition appears to be consistent with the general definition of "gross income" noted above: "total receipts ... before deducting expenditures for any purpose."

Section 18-54 of the Beaufort County Code clarifies the income to be used in calculating Beaufort County's license tax, as follows:

> No deductions from gross income shall be made, except income from business done wholly outside of the county jurisdiction on which a license tax is paid to another county or municipality, or income which cannot be taxed pursuant to state law. The applicant shall have the burden to establish the right to a deduction by satisfactory records and proof. No person shall be exempt from the requirements of this article by reason of the lack of an established place of business within the county, unless exempted by state or federal law. ... No person shall be exempt from this article by reason of the payment of any other tax, unless exempted by state law ....

In addition, section 18-69 clarifies that "[p]roperly apportioned gross income from interstate commerce shall be included in the gross income for every business subject to a business license tax."

Accordingly, it appears that all "gross receipts" not specifically excluded by ordinance and not exempted by other law should be reported to the county as the basis for its tax. Gay v. Ariail, 381 S.C. 341, 344-45, 673 S.E.2d 418, 420 (2009) ("All rules of statutory construction are subservient to the maxim that legislative intent must prevail if it can be reasonably discovered in the language used. ... If possible, legislative intent should be found in the plain language of the statute itself.").

Exemptions created by operation of other law

Section 4-9-30(12) of the South Carolina Code (1986 & Supp. 2011) provides the authority for Beaufort County's license tax and enumerates certain exemptions from that tax, as follows:

> Under each of the alternate forms of government listed in § 4-9-20 ...each county government within the authority granted by the Constitution and subject to the general law of this State shall have the following enumerated powers which shall be exercised by the respective governing bodies thereof:
>
> ....
>
> (12) to levy uniform license taxes upon persons and businesses engaged in or intending to engage in a business, occupation, or profession, in whole or in part, within the county but outside the corporate limits of a municipality except those persons who are engaged in the profession of teaching or who are ministers of the gospel and rabbis, except persons and businesses acting in the capacity of telephone, telegraph, gas and electric utilities, suppliers, or other utility regulated by the Public Service Commission and except an entity which is exempt from license tax under another law or a subsidiary or affiliate of any such exempt entity. No county license fee or tax may be levied on insurance companies. The license tax must be graduated according to the gross income of the person or business taxed. A business engaged in making loans secured by real estate is subject to the license tax only if it has premises located in the county but outside the corporate limits of a municipality. If the person or business taxed pays a license tax to another county or to a municipality, the gross income for the purpose of computing the tax must be reduced by the amount of gross income taxed in the other county or municipality.

As can be seen, section 4-9-30 exempts several persons and businesses from the operation of the county's business license tax, and it exempts "the amount of gross income taxed in [another] county or [in a] municipality." Additional income might be excluded by operation of other law. *E.g.*, Letter to Adelaide R. Bodie, Op. S.C. Att'y Gen. (Aug. 2, 1972) (opining that taxes imposed upon purchasers of certain products but collected by dealers of those products as agents of the government should be excluded from the calculation of the dealers' gross receipts). As a general rule, however, the burden is on the taxpayer to demonstrate that it is entitled to a claimed exemption. *E.g.*, Letter to Debbie Owens, Op. S.C. Att'y Gen. No. 84-140Att'y Gen. No. 84-140 (Dec. 21, 1984). [3]

Effect of an exemption from income tax

Via subsequent conversation, you have clarified that your particular concern is whether exemption from federal or state income tax will operate to exclude income from the county's business license tax. Because a business license tax is not a tax upon the income itself, income that is exempt from income tax will not necessarily be exempt from use in calculating a license tax. *Cf.* Hay v. Leonard, 212 S.C. 81, 97, 100, 46 S.E.2d 653, 660, 661 (1948) ("[T]he tax is not on the property itself; it is on the privilege of dealing with it. The value of such privilege is measured by the gross receipts therefrom ...."); Thomson Newspapers, Inc. v. City of Florence, 287 S.C. 305, 338 S.E.2d 324 (1985) (newspaper did not satisfy its burden to show a license tax was unconstitutional simply by showing that the newspaper's classification for purposes of the license tax differed from its classification for the purposes of income and *ad valorem* taxation); Letter to Joseph H. Earle, Jr., Op. S.C. Att'y Gen. No. 82-56Att'y Gen. No. 82-56 (Aug. 18, 1982) (explaining that an exemption from *ad valorem* taxation would not automatically exempt an entity from a business license tax). Rather, the terms of the ordinance will control, provided they are not inconsistent with constitutional or statutory law. [4]

By its plain language, the Beaufort County license tax ordinance does not mandate the use of income tax returns in calculating gross income. Instead, it references these returns only as a resource for verifying the income reported to the county. Beaufort County Code § 18-47 ("Gross income for business license purposes, [sic] may be verified by inspection of returns filed with the Internal Revenue Service, the South Carolina Department of Revenue ... or other government agency."); *id.* § 18-53(b) ("Applicants may be required to submit copies of state and federal income tax returns reflecting gross income figures."). For most businesses, the income to be reported to the county is defined by sections 18-47, 18-51, 18-54, and 18-69 of the Beaufort County Code—as quoted above—and these sections do not indicate that exemption from income tax will have any effect on the calculation of the county's license tax.

Nonetheless, it is worthy of note that some organizations or activities that are exempt from income tax might not qualify as "business" within the meaning of the Beaufort County license tax ordinance. See Beaufort County Code § 18-47 (defining the term "business" and explaining the circumstances under which an organization devoted to "charitable purposes" will be considered a business). [5] If an organization or activity is not "business," the receipts therefrom might not qualify as "gross receipts" for license tax purposes. *See id.* (defining gross receipts as the "total revenue of a business ..." and as "the value proceeding or accruing from the sale of tangible business personal property ...and all receipts, by reason of any business engaged in ..." (emphasis added)). Any ambiguity in construing these provisions should be resolved in favor of the taxpayer. Beard v. S.C. Tax Comm'n, 230 S.C. 357, 367, 95 S.E.2d 628, 634 (1956) ("It is a well-established rule of construction that a tax statute is not to be extended beyond the clear import of its language, and that any substantial doubt as to its meaning should be resolved against the government and in favor of the taxpayer."); *accord* Hay, 212 S.C. at 92, 46 S.E.2d at 658 (applying this rule in the context of a business license tax).

Conclusion

In sum, an exemption from state or federal income tax does not necessarily create an exemption from Beaufort County's business license tax. Rather, gross income for business license tax purposes should be calculated according to the definition in the license tax ordinance, provided that definition is not inconsistent with constitutional or statutory law.

Very truly yours,

/s/

Dana E. Hofferber

Assistant Attorney General

REVIEWED AND APPROVED BY:

/s/

Robert D. Cook

Deputy Attorney General

[1]

You have not inquired about the validity of the ordinance.

[2]

You have represented that the county's business license tax was amended most recently by Beaufort County Ordinance 2010/13 (Aug. 23, 2010), a copy of which you have provided to this Office. The definition of "gross receipts" in 2010/13 appears to be an adoption—with modifications—of the definition of "gross income" provided by a previous version of the county code. *See* Beaufort County Ordinance 99-36 (Nov. 22, 1999).

[3]

Section 12-20-110 of the South Carolina Code (2000 & Supp. 2011) exempts certain homeowners' associations from the corporate license fees imposed by that chapter. The section does not explicitly affect county license taxes.

[4]

Again, we assume for the purposes of this opinion that the ordinance is valid.

[5]

Section 18 -47 provides, in relevant part:

Business means a calling, occupation, profession or activity engaged in with the object of gain, benefit or advantage, either directly or indirectly. In addition to the above-described activities ... an individual shall be deemed to be in business if that individual owns and rents two (2) or more residential rental units ...within the county, excluding the municipalities therein. This applies to both short-term and long-term rentals.

Charitable [p]urpose means benevolent, philanthropic, patriotic, or eleemosynary purpose which does not result in personal gain to a sponsor, organizer, officer, director, trustee or person with ultimate control of the organization. [A] [c]haritable [organization shall be deemed a business subject to a license tax unless the entire net proceeds of its operation, after necessary expenses, are devoted to charitable purposes. Compensation in any form to a sponsor, organizer, officer, director, trustee or person with ultimate control of the organization shall not be deemed a necessary operating expense.

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2006 WL 1574907 (S.C.A.G.)

Office of the Attorney General
State of South Carolina

*1 May 26, 2006

The Honorable Gilda Cobb-Hunter
Member
House of Representatives
309-C Blatt Building
Columbia, South Carolina 29211

Dear Representative Cobb-Hunter:

We received your letter requesting an opinion regarding a municipality's authority to levy a local business license tax. You informed us:

> According to one of my constituents, the town of Holly Hill's business license tax is based on the business' gross income, instead of what the business nets. This method of computation differs from other municipalities in the area and places a serious hardship on business in Holly Hill.

Accordingly, you request an opinion as to whether "the municipality of Holly Hill has the Authority to tax business licenses based on the business' gross income, and if so, from what statute does its authority derive"?

Law/Analysis

"A municipal corporation is a creature of statute and has only the powers expressly granted it, those which are necessarily or fairly implied in or incident to the express powers, or those powers essential to the accomplishment of its purpose." Piedmont Pub. Serv. Dist. v. Cowart, 319 S.C. 124, 131, 459 S.E.2d 876, 880 (Ct. App. 1995). Article VIII, section 9 of the South Carolina Constitution (1976) provides, in part: "The structure and organization, powers, duties, functions, and responsibilities of the municipalities shall be established by general law...." In section 5-7-30 of the South Carolina Code (2004), the Legislature confers numerous powers upon municipalities, including the power to

> levy a business license tax on gross income, but a wholesaler delivering goods to retailers in a municipality is not subject to the business license tax unless he maintains within the corporate limits of the municipality a warehouse or mercantile establishment for the distribution of wholesale goods; and a business engaged in making loans secured by real estate is not subject to the business license tax unless it has premises located within the corporate limits of the municipality and no entity which is exempt from the license tax under another law nor a subsidiary or affiliate of an exempt entity is subject to the business license tax....

(emphasis added). Furthermore, our Supreme Court has stated: "the licensing power of municipalities is to be strictly construed and exercised in strict conformity with the terms of its grant." Southern Bell Tel. and Tel. Co. v. City of Aiken, 279 S.C. 269, 272, 306 S.E.2d 220, 222 (1983).

In accordance with the authorities cited above, it is our opinion that not only would Holly Hill be authorized to

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tax business licenses based on gross income, section 5-7-30 of the South Carolina Code appears to mandate this basis for taxation of business licences by a municipality.

Very Truly Yours,
Cydney M. Milling
Assistant Attorney General

REVIEWED AND APPROVED BY:

Robert D. Cook
Assistant Deputy Attorney General

2006 WL 1574907 (S.C.A.G.)

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1983 S.C. Op. Atty. Gen. 121, 1983 S.C. Op. Atty. Gen. No. 83-76, 1983 WL 142745 (S.C.A.G.)

Office of the Attorney General
State of South Carolina

Opinion No. 83-76

September 26, 1983

SUBJECT: Taxation, Municipal Ordinance, Business License Tax

Municipalities have been granted the specific authority to levy business license tax on gross income pursuant to § 5–7–30. Gross income is interpreted as total receipts from a business before deductions, but excluding those funds which are collected and held for remittance to another governmental entity.

TO: Honorable J. Ira Ruff
Mayor
Town of Leesville

QUESTION:
When interpreting the Business License Ordinance of the Town of Leesville, does the term 'gross income' for license tax purposes exclude the cost of goods sold?

APPLICABLE LAW:
Sections 5–7–30, 12–7–510, 12–7–660, 12–21–2420, and 12–27–10 of the South Carolina Code of Laws (1976).

DISCUSSION:
Municipalities have only powers expressly granted by the Legislature or necessarily implied from those so granted, Blake v. Walker, 23 S.C. 515. Section 5–7–30 gives municipal corporations specific powers. The exercise of these powers is subject, however, to limitations, McCoy v. York, 193 S.C. 390, 8 S.E. 2d 905.

Section 5–7–30 reads in pertinent part:

> 'All municipalities of the State shall, in addition to the powers conferred to their specific form of government, have authority to enact regulations, resolutions, and ordinances, not inconsistent with the Constitution and general law of this State, including * * * levy a business license tax on gross income, provided, however, that a wholesaler delivering goods to retailers in any municipality shall not be subject to the business license tax unless he maintains within the corporate limits of the municipality a mercantile establishment for the distribution of wholesale goods or a warehouse; * * *.'

Gross income means the total receipts from a business before deducting expenditures for any purpose. Columbia Ry. Etc. Co. v. Tax Commission, 119 S.C. 480, 112 S.E. 267 (1921). Net income is that portion of the receipts which remains after paying wages and paying for materials * * *. First Trust Co. of St. Paul v. Commonwealth Co., 98 F. 2d 27, 31 (1938). [See Attorney General's Opinion dated February 2, 1977]. Gross income becomes 'net' by deductions. Hamilton National Bank v. District of Columbia, 156 F. 2d 843 (1946).

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Section 12–27–10, Code, levies a gasoline tax against the consumer, to be collected by the dealer as an agent for the State.

Section 12–21–2420, Code, imposes an admissions tax on the person paying the admission price. The person collecting the admission price is also required to collect the admissions tax as an agent of the State Tax Commission.

Because the gasoline tax and the admissions tax are levied on the consumer, but collected by the business owner for remittance to the State, those funds are not to be included in gross income when computing the business license tax. (See Attorney General's Opinion No. 3356 dated August 2, 1972).

*2 Code § 12–35–510 imposes a four (4) percent tax on the gross proceeds of sales of a business. This tax is levied on the seller of goods but is collected from the purchaser. Because this tax is levied on the seller, those funds collected as sales taxes are to be included in gross income when computing the business license tax.

Section 4 of the ordinance of the Town of Leesville reads, in part, 'a license fee based on gross income for the preceding calendar or fiscal year * * *.' Section 6 reads, in part:

> 'No deductions from gross income shall be made except income from interstate commerce only, income from business done wholly outside of the Town on which a license tax is paid to some other municipality, or income which cannot be taxed pursuant to state law.'

Based on precedent, giving the term 'gross income' its common meaning, and strictly construing the ordinance as written, the Town of Leesville is permitted to compute the license fees on the total receipts of a business, before any deductions are taken. Those funds which are a tax upon the retail purchaser but collected and held by the owner/operator of the business for distribution to other governmental agencies are not to be included as receipts of the business.

CONCLUSION:

Gross income is interpreted as total receipts from a business before deductions, but excluding those funds which are collected and held for remittance to another governmental entity.

Arlene D. Hand
Assistant Attorney General

1983 S.C. Op. Atty. Gen. 121, 1983 S.C. Op. Atty. Gen. No. 83-76, 1983 WL 142745 (S.C.A.G.)

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Because the gasoline tax and the admissions tax are levied on the consumer, but collected by the business owner for remittance to the State, those funds are not to be included in gross income when computing the business license tax. (See Attorney General's Opinion No. 3356 dated August 2, 1972).

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Arlene D. Hand
Assistant Attorney General

1983 S.C. Op. Atty. Gen. 121, 1983 S.C. Op. Atty. Gen. No. 83-76, 1983 WL 142745 (S.C.A.G.)

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Office of the Attorney General
State of South Carolina

Opinion No. 77-40

February 2, 1977

Hon. M. Ernest Nunnery
Member
State House of Representatives District No. 44
State House
Columbia, South Carolina

Dear Representative Nunnery:

In response to your request for an opinion from this Office as to the meaning of the term 'gross income' as it appears in Section 47–32, CODE OF LAWS OF SOUTH CAROLINA, 1962, as amended (Cum. Supp.), my opinion is that the ordinary and common meaning is 'gross receipts' of a business before deductions or expenditures for any purpose. See, e.g., First Trust Co. of St. Paul v. Commonwealth Co., 98 F.2d 27 (8th Cir., 1938); Columbia Ry., Etc. Co. v. Tax Commission, 119 S.C. 480, 112 S.E. 267 (1921).

With kind regards,
Karen LeCraft Henderson
Assistant Attorney General

1977 S.C. Op. Atty. Gen. 42, 1977 S.C. Op. Atty. Gen. No. 77-40, 1977 WL 24383 (S.C.A.G.)

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Exhibit L

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State of South Carolina

In the Administrative Law Court

No. 10-ALJ-17-0270-CC

DUKE ENERGY CORPORATION,	)
	)
Petitioner,	)
	)
vs.	)
	)
SOUTH CAROLINA DEPARTMENT OF REVENUE,	)
	)
Respondent.	)

D E P O S I T I O N

WITNESS:	JOE SOUTHARD
DATE:	December 2, 2011
TIME:	9:00 a.m. - 12:50 p.m.
LOCATION:	Willoughby & Hoefer 930 Richland Street Columbia, South Carolina
TAKEN BY:	Attorney for the Petitioner
REPORTED BY:	KATHRYN J. LINDLER

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Q. And the State too? The State didn't have to sign it either?

A. The State didn't have to sign it. As I say it was a tool to help the auditor.

Q. Do you ever remember executing a waiver in one of your audits, Joe, where a taxpayer would seek a refund after the waiver was signed for that period?

A. I couldn't tell you. I don't --

Q. You don't remember that happening?

A. I don't remember that happening. They might have, but if they did, I don't recall.

Q. You don't recall that happening in one of your audits where a taxpayer sought a refund after signing?

A. I don't remember.

Q. You don't remember?

A. No.

Q. If a taxpayer were to seek a refund after signing a waiver, would you have told them that they couldn't seek a refund after signing the waiver?

A. No. I don't see why I would.

Q. You're familiar with I imagine based upon the training and keeping up to date with South Carolina law with South Carolina revenue procedures generally?

A. Generally.

Q. When a new one would come out, you would

Exhibit M

RECYCLED PAPER
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STATE OF SOUTH CAROLINA

ADMINISTRATIVE LAW COURT

DUKE ENERGY CORPORATION,

Petitioner(s),

vs. Case No: 10-ALJ-17-0270-CC

SOUTH CAROLINA DEPARTMENT OF REVENUE,

Respondent(s).

D E P O S I T I O N

WITNESS: RONALD W. URBAN

DATE: Wednesday, March 14, 2012

TIME: 10:30 a.m.

LOCATION: Willoughby & Hoefer, P.A.
930 Richland Street
Columbia, South Carolina

TAKEN BY: Attorneys for the Petitioner

REPORTED BY: SHERI L. BYERS
Registered Professional Reporter

- -

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Harry Cooper was the general counsel, and I was chief counsel.

Q. Okay.

A. And that stayed that way for I don't know how many years, but several years. And then I reported to Rick Handel for about six, seven months. Maybe longer than that, maybe 12 months. And then I reported to Nick Sykes, who was the general counsel for litigation. And then when Nick retired six months before I did, I was the -- I reported to Harry Cooper at that time, who was then the deputy director.

Q. Once again.

A. He was the deputy director then.

Q. When did you retire?

A. I retired April 1st, 2010.

Q. Okay. So are you aware that during the years 1978 through 2001, Duke Energy -- 1978 -- in the years leading up to this case, that Duke Energy was under audit by the South Carolina Department of Revenue for state income taxes?

A. I'm aware of that.

Q. Okay. And were you involved in that audit?

A. No.

Q. At any time after the audit was completed, did you become involved in the discussions with respect

A. Allegedly. I'm not agreeing and I won't agree that he is signing on behalf and representing that's the Tax Commission's position.

Q. Do you have any reason to believe that Marvin Davant, who signed this underneath where it says South Carolina Tax Commission, was not signing on behalf of the South Carolina Tax Commission?

A. Yes, because I don't have any -- I don't have any belief that he was acting on behalf of the Tax Commission when he did this.

Q. Fair enough. Okay.

I guess you would say the same thing for Duke Power Company; is that correct?

A. No. I don't know anything about Duke Power Company.

Q. Okay.

A. If that individual had the authority or not.

Q. Okay. And would you agree that both of those signatures are dated -- the first one for Duke Power Company is dated 11-16-93?

A. Correct.

Q. And the signature for the South Carolina Tax Commission is dated 10-19-93?

A. Correct.

Q. Okay. And this form, FS-43, this deals with

A. This refund means the Division is of the opinion that they can extend or waive the time for a refund.

Q. So the --

A. The Field Service Division. Marvin Davant's division.

Q. Well, let's take a step back. Let's assume that this -- that Marvin Davant never signed, that this FS-43 was just a blank form.

A. It's a field service form. That's what the FS stands for.

Q. Is that -- okay. What is Field Services?

A. That's Marvin Davant's department. They are the entity that audits, does field audits. But it is not a Tax Commission form. It says Tax Commission at the top, but that's not what it is.

Q. If you can answer the questions that I ask.

A. I'm sorry.

Q. Okay. So the Field Services Division, is that a division -- what is that within the -- what was that within the South Carolina Tax Commission?

MR. GREEN: Objection as to form.

THE WITNESS: It's an operating division within the Tax Commission.

BY MR. TRESH:

Q. Okay. And so is it -- and this form would allow a refund, correct, by the taxpayer?

A. Allegedly it would allow a refund according to Marvin Davant.

Q. Okay. Again, who signed on behalf of the South Carolina Tax Commission?

A. That way he signed it, I don't know if he had it. There was no Tax Commission in existence, first of all, in 1996. And so I don't know why they were using this form to begin with since there was no Tax Commission. So Marvin signed it. You would have to ask Marvin who he was signing it for.

Q. Okay. Is it your position that Marvin Davant, who signed both of these forms, signed them without the knowledge of his superiors within the South Carolina Tax Commission?

A. Yes.

Q. Okay. And that this form -- is it your testimony that this form FS-43 was issued to taxpayers without the knowledge of others within the South Carolina Tax Commission, that Marvin Davant was acting in a rogue manner, and nobody knew this was going on?

A. When you say "others," who do you mean?

Q. His bosses.

A. The commissioners, yes. I'm not saying he operated in a rogue manner, but I'm saying he signed this without the knowledge of the commissioners.

Q. Harry Cooper had no idea --

A. Correct.

Q. -- that these forms were being issued?

A. Correct.

Q. Did Marvin Davant ever go through any disciplinary procedures about issuing these forms, to your knowledge?

A. Not to my knowledge.

Q. Okay. Did anybody in South Carolina Department of Revenue or the South Carolina Tax Commission, to your knowledge, ever tell Marvin Davant that he did not have authority to sign these forms?

A. I don't know.

Q. While you were at the South Carolina Department of Revenue through 2010, you said you were called in to a meeting about this case, correct?

A. That's correct.

Q. And was the issue of these waivers discussed in that meeting?

A. Yes.

Q. Why wasn't Marvin Davant disciplined?

A. Marvin was gone. He's retired.

document.

What was the effect of this paragraph that says, "This agreement extends the time for the mailing --" "-- for mailing the notice of assessment or refund of the above tax pursuant to the provisions of 12-54-80 of the 1976 South Carolina Code of Laws as amended."

Would it have been your understanding that in 1996 the taxpayer would have been able to -- that this extended the time for the taxpayer to file a refund?

A. Not for the years -- probably in -- well, let's see. Let me tell you how I think it would work. And first of all, obviously, they're still using a -- I don't know where they got the form, but, again, it's referring to the wrong statutes and has the wrong heading there.

But this is what they could do back in 1996. Marvin could have granted an extension under 12-60-40 that would allow for refunds for any of the -- any of the tax years who had not yet expired. So even though it was enacted in '95, I don't think '94 had expired yet and probably 1993 hadn't expired. And I don't know about '92. So he could have extended the time in which to put a claim for refund in for those years, '92, '93, '94. I think.

Q. Okay.

A. I mean, you can run the numbers and see that.
Q. Okay.
A. But it looks backwards, you know, to those statutes that had not yet expired.
Q. Okay. So your view is Marvin could have extended the time for Duke to file a refund claim from years that were open?
A. That's correct.
Q. '92, '93, what have you, through the current period?
A. I think so. I mean, I know that's what the law is. I just don't know if those things that had expired at the time Marvin -- and those years expired at the time Marvin executed this.
Q. That's why I'm saying those years that were open.
A. Yeah.
Q. Okay. That would be your view.
Let's turn back, then, to the prior document that was executed in 1993. It uses the exact same language in the middle of the page there. "This agreement extends the time for mailing Notice of Assessment."
Why would this form have used that language, the same exact language that's in the form that you

clear the Department's policy that a waiver -- that the Department had the ability to extend the time for taxpayers to file a refund claim using a waiver form; is that correct?

MR. GREEN: Objection as to form.

THE WITNESS: I don't know if it says waiver form in there or anything, but it does specifically say that they now have to authority under 12-40-60 -- or excuse me, 12-60-40.

BY MR. TRESH:

Q. Okay.

A. Clearly states that.

MR. TRESH: Okay. Let's go to the procedural bulletin.

(PETITIONER'S EXH. 5, S.C. Revenue Procedural Bulletin #00-3, was marked for identification.)

BY MR. TRESH:

Q. I've now haded handed you a copy of South Carolina Revenue Procedural Bulletin 00-3. Subject matter is Claims for Refund and Correction of Errors in Tax Years Barred by Time Limitations; is that correct?

A. That's correct.

Q. Are you familiar with this document?

A. Yes, I am.

Q. Were you the author of this document?

A. No, I wasn't.

Q. Did you review this document before it was issued?

A. I probably did because it would have been, again, like the previous document, it would have been e-mailed around the Department before it was issued.

Q. Okay. And this document, in terms of -- in section -- I believe page 4, bottom of the page. It states, "Consistent with its longstanding administrative position, the Department will continue to interpret the time limitations in Code Section 12-54-85 consistent with the following rules."

Correct?

A. Correct.

Q. And then it goes on to state what those rules were.

Given that you're familiar with the document, what would your view of these rules be?

A. I would take it to mean when 12-54-85 was enacted in 1995, the Commission had consistently followed 12-54-85 as, you know, after its enactment as it states here. I believe that's what it's saying.

Q. And is this still the current policy of the Department with respect to waivers to the best of your

in your role as chief counsel, correct?

A. Should have been, yes.

Q. Okay. When this TAM 89-3 was issued, would a TAM typically have been shared with employees of the Department?

A. I believe so.

Q. Would a TAM have been shared with Marvin Davant in his role as director of Field Services?

A. Yes, it would have been.

Q. And so the TAM was issued in 1989, and we have before us at least one waiver that was signed -- examplar that was signed in 1993?

A. Correct.

Q. And so even though Marvin Davant was director of Field Services who reported to Harry Cooper, fairly senior person within the Department of Revenue, Marvin would have been aware of the '89 TAM, yet he was still issuing form SF-43s, which you claim are inconsistent with the TAM?

A. That's correct. And he would have been reporting in '89 probably to Greg Frampton, not Harry Cooper, probably.

Q. So Harry would have known the TAM and in your view was intentionally disregarding it?

A. Correct. I can't say he knew of it, but he

was not following probably what the guides in the TAM was stating.

Q. But it would have been common, you would have expected Marvin to have received a copy of the TAM?

A. Marvin would have received a copy of the TAM just like with the other documents because they -- I don't know if in '89 they were displayed on the computer at that time, but they would have been circulated. And Marvin was much higher than I was at that time. Not much higher, but higher. And if I was getting them, he would have got one.

Q. Can you tell me your understanding of the 1989 TAM.

A. The '89 TAM dealt with the school teacher, retired school teacher who had retired in South Carolina. And I think she was asking if her income was subject to income -- she asked somebody if she had to file tax returns and report it to South Carolina.

And somebody at the Department of Revenue -- well, then the Tax Commission told her yes. And I think she alleges it happened on more than one occasion. And it was too late to put a claim for a refund in. And so she was asking if the Tax Commission waive the time limitation so that she could get her

Exhibit N

RECYCLED PAPER
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State of South Carolina
Department of Revenue
Office of General Counsel for Litigation
301 Gervais Street, P.O. Box 12265, Columbia, South Carolina 29211
Telephone (803) 898-5130 Telecopier (803) 898-5147

February 4, 2010

Burnet R. Maybank, III, Esquire
James F. Reames, III, Esquire
Nexsen Pruet, LLC
PO Drawer 2426
Columbia, SC 29202

Re: Department Determination
Duke Energy Corporation

Dear Messrs. Maybank and Reames:

Enclosed is the South Carolina Department of Revenue's Determination in the above-referenced matter. If you disagree with the Determination, you may request a contested case hearing before an Administrative Law Judge. If you choose to pursue such remedy, you must do so within 30 days of the date of this letter. If you fail to respond within this time limitation, you will lose your right to appeal the Department Determination and your protest will be ended. Should you desire a contested case hearing, you must complete the enclosed request form and mail it, along with a $100 filing fee, to the Administrative Law Court at the address stated on the form's instruction sheet.

The Administrative Law Court rules require that you also send me a copy of your request. My address is as follows: PO Box 12265, Columbia, SC 29211.

Yours truly,

OFFICE OF GENERAL COUNSEL FOR LITIGATION

Michael S. Traynham
Counsel for Litigation

MST:lbc
Enclosures

DEPARTMENT DETERMINATION

Taxpayer:

Duke Energy Corporation
PO Box 1642
Houston, TX 77251-1642

Periods Involved:

Corporate Income Tax Years 1978 through 2001

Matters in Dispute:

1. Is the taxpayer entitled to utilize a single gross receipts factor apportionment formula in the calculation of its South Carolina corporate income tax?

2. Is the taxpayer entitled to include return of principal from the sale of short-term financial instruments in the denominator of its gross receipts factor?

3. Is the taxpayer's claim for refund timely?

Refund amount at issue:

Duke Income Tax:	$125,142,447.
Crescent Income Tax:	1,098,198.
Total:	$126,240,645.*

*Total is exclusive of interest. Any refund owed would be subject to a statutory interest rate pursuant to S.C. Code Ann. § 12-54-25 (Supp. 2008)

Determinations:

1. The taxpayer is not entitled to utilize a single-factor formula for apportioning its taxable income.

2. The taxpayer may not include its return of principal from the sale of short-term investments in calculating its gross receipts factor.

3. The taxpayer's claim for refund is untimely for some of the periods in question.

Relevant Facts:

1. Duke Energy Corporation (Duke or taxpayer), formerly known as Duke Power Company, is a multi-state power provider with operations in South Carolina.

2. In December 2002, Duke filed amended South Carolina corporate income tax returns for income tax years 1978 through 2001 requesting a substantial refund.

3. The taxpayer relied on waivers of the statutory time limit for filing amended returns (taxpayer's claim for refund). These waivers were provided by an employee of the Department of Revenue (Department) due to ongoing audit issues. The first of these waivers was issued on August 16, 1988.

4. The taxpayer raised three primary arguments in support of its claim for refund; (A) the taxpayer is not required to calculate its income tax on a three-factor formula pursuant to S.C. Code Ann. § 12-6-2250 (2008); (B) the taxpayer is entitled to include sales of short-term investments in the denominator of its gross receipts factor; and (C) the income and expense of Crescent Resource Corporation was not properly allocated in the original return.

5. The Department denied the requested refunds by letter dated February 12, 2003.

6. The taxpayer filed a timely protest of this denial by letter dated March 12, 2003.

Analysis:

1. The taxpayer is not entitled to use a single-factor gross receipts formula.

Pursuant to S.C. Code Ann. § 12-6-2290 (Supp. 2008), "[i]f the principal profits or income of a taxpayer are derived from sources other than those described in Section 12-6-2250 or Section 12-6-2310,"[1] the taxpayer must utilize a single factor apportionment ratio (gross receipts formula). The taxpayer argues it is entitled to utilize this formula because it is not a taxpayer described in either of the other code sections referenced by § 12-6-2290.

Section 12-6-2250(A) provides as follows:

> A taxpayer whose principal business in this State is (i) manufacturing or a form of collecting, buying, assembling, or processing goods and materials within this State, or (ii) selling, distributing, or dealing in tangible personal property within this State, shall make returns and pay annually an income tax that includes its income apportioned to this State. Its income apportioned to this State is determined by multiplying the net income remaining after allocation pursuant to Sections 12-6-2220 and 12-6-2230 by a fraction, the numerator of which is the property ratio, plus the payroll ratio, plus twice the sales

[1] S.C. Code Ann. § 12-6-2310 (2000) is not relevant to the facts of this case.

> ratio, and the denominator of which is four. However, where the sales ratio does not exist, the denominator of the fraction is the number of existing ratios, and where the sales ratio exists but the payroll ratio or the property ratio does not exist, the denominator of the fraction is the number of existing ratios plus one. The property, payroll, and sales ratios must be determined in accordance with Sections 12-6-2260, 12-6-2270, and 12-6-2280, respectively.

(Emphasis added). The taxpayer's contention that it is not described by § 12-6-2250 is incorrect. The taxpayer is a manufacturer within the meaning of the statute, and must apportion its income according to the prescribed three-factor formula.[2] It has long been held in South Carolina that "a company engaged in the business of generating electricity is a 'manufacturer within the meaning of a Statute imposing a tax upon a 'corporation engaged in the business of manufacturing.'" Duke Power Co. v. Bell, 156 S.C. 299, 152 S.E. 865, 868 (1930). South Carolina is hardly alone in this assessment. See, e.g., Hetherington v. Camp Bird Co., 202 P. 1087, 1088, (Colo. 1922); Curry v. Alabama Power Co., 8 So.2d 521 (Ala. 1942); Minn. Power & Light Co. v. Pers. Prop. Tax, Taxing Dist., City of Fraser, Sch. Dist. No. 695, 182 N.W.2d 685, 691 (Minn. 1970). The taxpayer's statements to the public are replete with references to its power generating assets, and its focus on generating power more efficiently. See, e.g., Duke Energy 2008 Summary Annual Report. Put plainly, South Carolina law has long recognized that electricity is something that must be "manufactured" within the meaning of our tax laws, and the generating entity – the taxpayer, in this instance – is the electricity manufacturer. The taxpayer's argument that it is entitled to use a single-factor formula must be rejected.

II. The taxpayer is not entitled to include gross receipts from the sale of short-term investments in calculating its gross receipts or sales factor.

If the Department is correct, and the taxpayer must use the three-factor formula provided by § 12-6-2250, there remains the issue of how it must then calculate its apportionment ratio. The taxpayer argues that it may include all proceeds from short-term investments, including the return of principal, in the denominator of its gross receipts ratio. This argument would apply to the sales factor of the three-factor formula as well. In calculating the sales factor, S.C. Code Ann. § 12-6-2280 (2000) provides that:

> (A) The sales factor is a fraction in which the numerator is the total sales of the taxpayer in this State during the

[2] Moreover, the taxpayer's contention that it does not sell tangible personal property should also fail. "Tangible personal property" is specifically defined to include "services [such as] sales of electricity." S.C. Code Ann. § 12-36-60 (2000). Thus, while the taxpayer is correct that it provides a service, its service is statutorily defined as tangible personal property

taxable year and the denominator is the total sales of the taxpayer everywhere during the taxable year.

(B) The term "sales in this State" includes sales of goods, merchandise, or property received by a purchaser in this State other than the United States Government. The place where goods are received by the purchaser after all transportation is completed is considered the place at which the goods are received by the purchaser. Direct delivery into this State by the taxpayer to a person designated by a purchaser constitutes delivery to the purchaser in this State.

(C) The word "sales" includes, but is not limited to:

(1) rentals from tangible personal property located in this State which are not separately allocated; and

(2) sales of intangible personal property and receipts from services if the entire income producing activity is within this State. If the income-producing activity is performed partly within and partly without this State, sales are attributable to this State to the extent the income-producing activity is performed within this State.

Based on the calculation of the sales factor, the higher the denominator (total sales from everywhere) results in a lower sales factor which, in turn, results in less income tax owed the state.

The taxpayer has diluted its sales factor by including in its denominator (total sales from everywhere) the return of principal from its short-term investments. As part of its treasury and cash management program, the taxpayer invested in short-term investments for which it received a gain on the investments plus the return of principal. In so doing, taxpayer properly included the interest and gains related to the return from these investments in the denominator of the sales factor. However, by also including the return of principal in the denominator of its sales ratio, the ratio is diluted.

The following language was added to this section effective for tax years beginning after 2006:[3]

[3]Subsection (c) was also rewritten to discuss sales made to the United States Government.

> (D) For purposes of this section, items included in sales are as provided in Section 12-6-2295. Section 12-6-2295 provides in part:
>
> (B) The terms "sales" as used in Section 12-6-2280 and "gross receipts" as used in Section 12-6-2290 do not include:
>
> (1) repayment, maturity, or redemption of the principal of a loan, bond, or mutual fund or certificate of deposit or similar marketable instrument;

While the statute did not directly speak to the issue prior to 2006, the Department had implemented the long standing administrative practice to include only the net proceeds from investment activities. Income Tax Decision 1-D-309 (June 30, 1982) addressed the issue and concluded:

> The commission has included royalties and sales of business connected tangible and intangible property in the sales factor. However, sales of tangible and intangible business connected property have been included only to the extent that the sale resulted in a gain. To include the gross sales price tends to distort the sales factor. Thus, through prudent administrative practice, this procedure has been developed.
>
> All that is required of an apportionment formula is that is [sic] provide a reasonable approximation, Covington Fabrics v. South Carolina Tax Commission, 264 S.C. 59, 212 S.E.2d 574 (1975). The Income Tax Division's computation provides a reasonable basis for apportioning income and is thus valid . . ..

Again in 1988 in Income Tax Decision 1-D-88-11, the practice was reaffirmed. The taxpayer in that matter sought to include the entire proceeds from the sale of foreign exchange contracts. The finding concluded:

> The Division has included in the denominator of the sales factor gain resulting from the disposition of the exchange contracts. We find such to be proper. This position has been the practice of the Tax Commission since 1977 and is a longstanding administrative position. Such should not be overturned unless cogent reasons for doing so are found. Emerson Electric Co. v. Wasson, 287 S.C. 394, 339 S.E.2d 118 (1986). We find no cogent reasons to change the practice. It must be noted that the apportionment formula

> need not be an exact measure of the taxpayer's business activity but rather must only provide a reasonable approximation. Covington Fabrics v. South Carolina Tax Commission, 264 S.C. 59, 212 S.E.2d 574 (1975). Here inclusion of the gain from the foreign exchange contracts provides a reasonable apportionment approach.

Perhaps the leading case addressing this issue is American Telephone and Telegraph Company v. Director, Division of Taxation, 476 A.2d 800 (1984), cert. denied, 97 NJ 627, 483 A.2d 157 (1984) (AT&T). In AT&T, the court was concerned with the proper treatment of revenues received by AT&T from "investments made with its idle cash" under the New Jersey receipts fraction for its apportionment formula.[4] The New Jersey receipts fraction divides "New Jersey related receipts from sales, services, etc." by the "total receipts of taxpayer from sales, services, etc." AT&T argued that all revenues from its sale of short-term investments, including returns of principal, should be included in the sale of its short-term obligations, in the receipts fraction.[5] The court concluded that the term "receipts" for apportionment purposes was limited to the net gain from the sale or redemption of investment paper stating:

> We uphold as a general matter the exclusion of gross revenues received by plaintiff from the sale or maturity of investment paper. As Judge Crabtree observed, idle cash can be turned over repeatedly by investment in short term securities. It is no true reflection of the scope of AT&T's business done within and without New Jersey to allocate to the numerator or the denominator of the receipts fraction the full amount of money returned to AT&T upon the sale or redemption of investment paper. To include such receipts in the fraction would be comparable to measuring business activity by the amount of money that a taxpayer repeatedly deposited and withdrew from its own bank account. The bulk of funds flowing back to AT&T from investment paper was simply its own money. Whatever other justification there is for excluding such revenues from the receipts fraction, it is sufficient to say that to do otherwise produces an absurd interpretation of § 6(B). "It is axiomatic that a statute will not be construed to lead to

[4]The court gave the following explanation of "idle cash": "AT&T maintained a pool of funds which it received primarily as dividends from its subsidiary corporations and from the sale of stock and debt obligations. Money not needed for immediate business use was placed in certificates of deposit or invested in short term obligations of various types."

[5]The New Jersey Division of Taxation took the position that only interest owed on the investments should be included in the receipts fraction.

> absurd results. All rules of construction are subordinate to that obvious proposition. [Even the rule of strict construction] does not mean that a ridiculous result shall be reached because some ingenious path may be found to that end." State v. Provenzano, 34 N.J. 318, 322, 169 A.2d 135 (1961).

Of particular significance is the AT&T court's observation that including the full amount of money returned on the sale of short-term investments without the exclusion of principal would be comparable to "measuring business activity by the amount of money that a taxpayer repeatedly deposited and withdrew from its own bank account." Given that a return of principal on an investment is simply a return of the taxpayer's own money, to allow a taxpayer to recognize the return of principal in the gross receipts factor creates the anomaly that the taxpayer is being allowed to reduce its state taxable income not because of a decrease in business activity in the state but because of the amount of its own money the taxpayer has turned over during the tax period. See also, Sherwin-Williams Company v. Indiana Department of State Revenue, 673 N.E.2d 849 (1996) ("[T]his Court holds that 'gross receipts' for the purposes of the sales factor includes only interest income, and not the rolled over capital or return of principal, realized for the sale of investment securities.").

In Walgreen Arizona Drug Company v. Arizona Department of Revenue, 97 P.3d 896 (2004), the Arizona Court of Appeals cited with favor the opinion of an Arizona Tax Court, which had ruled that the return of principal on short-term investments did not qualify as gross receipts for the state's sales factor:

> [D]aily revenue from Walgreen's sales would be considered gross receipts when received. Any excess revenue after payment of debt or other disbursements remains a part of those gross receipts and should be counted as such. However, once that excess revenue is invested in securities or other interest bearing mediums, it loses its characterization as gross receipts and may not be counted a second time as gross receipts simply because the money was withdrawn from an investment in a marketable security or interest bearing account. This is akin to someone taking the $100 left from their [sic] weekly paycheck[,] which is considered income when it was received, depositing it into an interest bearing account[,] then withdrawing the $100 one month later and claiming it as income a second time. That $100 is not income.

In affirming the ruling of the tax court, the Walgreen court, quoting extensively from the N.J. AT&T case, held that "the return of principal from the type of short-term

investments at issue here is not includable in the sales factor denominator calculated pursuant to A.R.S. Section 43-1145." Walgreen, 97 P.3d at 902.[6]

The taxpayer has argued that the term "sales" includes "sales of intangible personal property . . ." and, thus, would include the proceeds from the sale of short-term investments. However, when the effect of including the return on principal in the gross receipts factor is considered, there is room to go beyond the language. In Kiriakides v. United Artists Communications, Inc., 312 S.C. 271, 440 S.E.2d 364 (1994), the Supreme Court commented thusly on the strict construction of statutes:

> However plain the ordinary meaning of the words used in a statute may be, the courts will reject that meaning when to accept it would lead to a result so plainly absurd that it could not possibly have been intended by the Legislature or would defeat the plain legislative intention . . .. If possible, the court will construe the statute so as to escape the absurdity and carry the intention into effect.

Based upon the reasoning employed by the New Jersey AT&T and Walgreen courts and the Department's longstanding administrative practice, a taxpayer's return of principal should not be included in the sales factor. Inasmuch as the principal "sales" at issue here are nothing more than an exchange of the taxpayer's own money, they have no substance other than to artificially inflate the denominator of the gross receipts formula, which in turn serves to decrease South Carolina income tax owed. To allow the return on principal to be included in the sales factor, when to do so lessens the South Carolina income subject to tax, and as a consequence unreasonably represents the amount of business done in South Carolina, is plainly absurd as contemplated by the Kiriakides court.[7] Thus, the return of principal is not properly includable in calculating the taxpayer's South Carolina sales factor.[8]

---

[6]The Walgreen court also cited a regulation promulgated by the Multi-State Tax Commission (MTVC), which defines "gross receipts" to exclude the return of principal on short-term investments. Walgreen, 97 P.3 at 901. See MTC Reg. IV.2(a)(5).

[7]Even in those several cases wherein the deciding court has found that the return of principal is included in "sales" or "gross receipts", those courts have determined that the use of an alternative apportionment formula is appropriate in order to fairly represent the extent of the taxpayer's business within that state. Thus, the return on principal was ultimately excluded from the sales or gross receipts under an alternative apportionment methodology.

[8]In the alternative, the Department could argue that the return of principal should be excluded from the sales factor based on an alternative apportionment formula found in § 12-21-2320(A) as this would more fairly represent the taxpayer's business in South

III. Timeliness of the taxpayer's claim for refund.

A. The waivers provided to the taxpayer are not intended to extend the time for filing a claim for refund.

The taxpayer's refund claim extends over a period of more than 20 years, from 1978 to 2001. In support of its claim, the taxpayer provided numerous copies of waivers provided by a Department employee periodically during that period. These waivers are titled "Consent to Extend the Time to Assess Tax." The language of the waivers state that the agreement "extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of [the South Carolina Code]." The waivers cite different code provisions depending on when they were issued, but all cited code provisions refer to the Department authority, with a taxpayer's consent, to extend the time for assessing a tax. See S.C. Code Ann. § 12-54-85(C)(4) (Supp. 2008). The waivers are not intended to extend the time in which a taxpayer can file a claim for refund. If the Department's examination of a taxpayer reveals that a refund is due, it will be paid, but nothing in the waiver itself grants the taxpayer an extension of time to file a refund claim. Thus, the taxpayer is still constrained by the time limitations for filing a refund contained in § 12-54-85(F), discussed more fully below. Thus, the only years for which the taxpayer's refund claim is timely are 2001, 2000, and 1999.

B. The Department had no authority to extend the time for filing a refund claim before the passage of the Revenue Procedures Act in 1995.

South Carolina law prescribes strict time limitations on the filing of a claim for refund. "Except [in cases involving Internal Revenue Service adjustments,] claims for credit or refund must be filed within three years from the time the return was filed, or two years from the date the tax was paid, whichever is later." Section 12-54-85(F)(1). The General Assembly granted the Department the authority to "extend time limitations provided by [Title 12]" with the passage of the Revenue Procedures Act (RPA) in 1995. S.C. Code Ann. § 12-60-40 (Supp. 2008). Prior to the passage of the RPA, the Department had no statutory authority to extend the time for a taxpayer to claim a refund – only the authority to extend the time for assessing a tax. See, e.g., S.C. Code Ann. § 12-54-80 (Supp. 1988).

Since the Department had no authority to extend the period for filing a refund until 1995, those periods which expired prior to that time could not have been extended by the Department even if the waivers operate as the taxpayer claims. Thus, regardless of what was intended by the Department's waivers, the taxpayer's refund claims for years prior to 1992 cannot be considered timely by the Department.

Carolina. This is the approach that some state courts have taken upon declining to rule that gross receipts do not include the return on short-term investments.

C. The Department cannot extend a filing period which has already expired.

Even if the waivers operate as the taxpayer believes, and the Department's authority to extend the time to assess tax permits it to also extend the time for the filing of a claim for refund by a taxpayer, the Department cannot extend a time period which has already expired. Extensions may only occur, with the taxpayer's consent, only within the period the Department is statutorily authorized to assess tax. See § 12-54-85(C)(4); see also § 12-54-80. The earliest waiver produced by the taxpayer was issued in August of 1988. That waiver could only extend the period for assessing taxes for any period still open under the three year statute of limitations.[9] Thus, the Department could not extend the time for assessing tax years 1978 through 1983. As a result, the claim for refund as to these years is not timely.

D. The taxpayer's 1998 claim for refund for Crescent Resources is not timely.

The taxpayer filed a claim for refund on behalf of Crescent Resources Corporation for tax years 1998 and 1999. Crescent was a separate entity at this time and apparently received no waivers to extend its time to file refunds, thus a claim for refund for Crescent is subject to the standard statute of limitations. Section 12-54-85(F). Based on the three year statutory look back period, the claim for 1998 is not timely, and cannot be granted by the Department.

February 4, 2010

[9]Moreover, the 1988 waiver only purported to extend the periods for tax years ending December 31, 1983 and later. The prior years were not referenced in a Department waiver until the mid 1990s.

Exhibit O

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STATE OF SOUTH CAROLINA

ADMINISTRATIVE LAW COURT

DUKE ENERGY CORPORATION,

Petitioner(s),

vs. Case No: 10-ALJ-17-0270-CC

SOUTH CAROLINA DEPARTMENT OF REVENUE,

Respondent(s).

D E P O S I T I O N

WITNESS: DR. IOANNIS "JOHN" PAPAPOLYMEROU

DATE: Wednesday, January 11, 2012

TIME: 10:27 a.m.

LOCATION: Nexsen Pruet, LLC
1230 Main Street, 7th Floor
Columbia, South Carolina

TAKEN BY: Attorneys for the Respondent

REPORTED BY: SHERI L. BYERS
Registered Professional Reporter

- -

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Energy provides is a service." and you described that service as transforming energy from one form to another.

Why do you conclude that what Duke energy provides is a service?

A. I conclude that it is a service because Duke Energy is not, you know, providing something in material form as is an object. So in my opinion, transforming energy from one form to the other is a service.

Q. Okay. Is that -- is that substantially based upon your conclusion, then, that electricity is not tangible personal property?

A. That's correct.

Q. What is the electricity or electromagnetic field that Duke Energy provides? What is that? It's not -- your conclusion is it is not tangible personal property?

A. Correct.

Q. What is it?

A. It's something intangible. It's a field.

Q. So you believe it is an intangible property?

A. No, it is intangible.

Q. Okay. So it's intangible, but it is not property?

Exhibit P

625

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STATE OF SOUTH CAROLINA

ADMINISTRATIVE LAW COURT

DUKE ENERGY CORPORATION,

Petitioner(s),

vs. Case No: 10-ALJ-17-0270-CC

SOUTH CAROLINA DEPARTMENT OF REVENUE,

Respondent(s).

D E P O S I T I O N

WITNESS: GLENN J. ROBINSON, M.S., P.E.

DATE: Wednesday, January 4, 2012

TIME: 10:31 a.m.

LOCATION: Willoughby & Hoefer, P.A.
930 Richland Street
Columbia, South Carolina

TAKEN BY: Attorneys for the Petitioner

REPORTED BY: SHERI L. BYERS
Registered Professional Reporter

- -

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only ask that if there is a question pending, you answer the question before we break.

Do you understand?

A. Yes.

Q. Do you have any questions before we get started?

A. No.

Q. Is there any reason that you are unable to respond completely and truthfully to the questions I ask you today?

A. No.

Q. What is your understanding of what you are here to testify about?

A. My understanding is that the matter under dispute is the method of taxation of Duke Energy. I have been asked by the Department of Revenue to provide some opinions regarding the nature of electricity, electrical generation, electricity and commerce. And I have done some work along those lines for them.

Q. Okay. In the deposition notice that you received, it indicates that you are going to testify to the principles of manufacturing of electricity; is that correct?

A. Yes, that's correct.

Q. And that you're going to testify as to its

correct?

A. Yes.

Q. Okay. So they can be metered. And you also testified that if something can be metered, it's a material?

A. No.

Q. That's not true?

A. Because right in front of you, I would conclude that a product, other than hours of service, can be metered, it is the result of manufacturing, not service. So if you want to go into hours of service, then, no, it's not manufactured. But if you're paying by quantity of goods transferred, then it is manufactured.

Q. So if I could buy cell phone service in some other way than hours of service, which I can.

A. Yes. You can do a flat rate.

Q. Right.

A. So could Duke. Duke could charge me $30 a month, and I could use as little or as much as I want. That would be a service. That would be definitely a service.

Q. Okay. So in your view, electricity -- the electricity that Duke sells, the electric energy that Duke sells, it would change from a material to a

service if Duke went ahead and sold it on a single charge, you know, $40 per month for all the electricity?

A. All you can eat.

Q. That's a service?

A. All you can eat. For example, a good example at a restaurant because I brought it up.

Q. Yeah.

A. Okay. Normally, you would think that's a material transfer. But if it's just a matter of you sit there and eat all you want and I'll charge you 10 bucks, that's transformed into a service.

Q. The manner in which you bill for something changes its --

A. Sure.

Q. -- characteristic?

A. For example, my garbage pickup. I pay them once a month. They take as little or as much as I produce. That's a service. No question.

Q. Okay.

A. And by the way, a lot of garbage companies will charge their commercial clients on a ton basis. Tons transfer. Okay. Well, that's different. Then it is a transfer of a commoditized product.

MR. TRESH: Can we take like a five-minute

Exhibit Q

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North Carolina Department of Revenue

COPY

Michael F. Easley
Governor

E. Norris Tolson
Secretary

February 9, 2007

Mr. Cam Brawley
ERNST & YOUNG
3200 Beechleaf Court, Suite 700
P.O. Box 40789
Raleigh, North Carolina 27629-0789

Re: Request for Private Letter Ruling – Nexus Issue

Dear Mr. Brawley:

This letter is in response to your letter dated January 12, 2007, wherein you requested that the North Carolina Department of Revenue ("Department") provide written guidance regarding its treatment for corporate income tax purposes of companies engaged in the sale of electricity or natural gas. The facts submitted for our consideration are as follows:

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QUESTIONS/RULINGS REQUESTED

1. Does North Carolina consider the sale of electricity as the sale of tangible personal property, intangible personal property, or a service for income tax purposes?

   Department's Response: For corporate income tax purposes, North Carolina does not consider the sale of electricity as the sale of tangible personal property. Receipts from the sale of electricity by a generator are sourced for corporate income apportionment purposes as receipts from sales of a service. Although the Department is on record in some non-Department of Revenue publications as treating electricity as tangible property for corporate income tax purposes, this position is incorrect. The correct apportionment methodology, which treats the sale of electricity as a sale of a service, will apply.

2. Does the Company have a corporate income tax filing requirement under North Carolina statute? If so, why?

   Department's Response: Yes. The company does have nexus in North Carolina for corporate income and franchise tax purposes since it has employees in this State engaged in non-protected activities on different occasions. However, if it is determined that the Company is a "public utility" as defined in G.S. 105-130.4(a)(6) and the Company's income producing activities take place completely outside of North Carolina, then the Company would not have an apportionment factor. Thus, Company does have a filing requirement, but its tax liability will most likely be limited to the minimum franchise tax of $35.

3. If the Company were domiciled in North Carolina and its only connection/presence outside of North Carolina was similar to the activities described in this ruling request, would the Company have the

right to apportion its income?

Department's Response: Yes. If the Company is engaged in unprotected activities outside of North Carolina, the Company would have the right to apportion its income pursuant to G.S. 105-130.4. However, if all of the Company's income producing activities take place in North Carolina, then 100% of the gross receipts should be attributed to this State and the numerator of the sales factor even though the Company may technically have the right to apportion.

4. If the Company has a filing requirement, would the sales factor only be used for apportionment?

   Department's Response: Yes. If the Company qualifies as a public utility under G.S. 105-130.4(a)(6) and has a filing requirement, then it would be required to utilize a single sales factor formula for apportionment purposes.

5. If the Company has a filing requirement, how are the sales of the Company sourced to the state under North Carolina statute?

   Department's Response: The receipts from the sales of a service are in North Carolina if the income-producing activity is performed in the State. [G.S. 105-130.4(l)(3)(c)] The sale of gas is considered to be a sale of tangible personal property, therefore gas sales would be sourced to North Carolina if the gas is received in North Carolina.

This ruling is based solely on the facts submitted to the Department of Revenue for consideration of the transactions described. If the facts and circumstances given are not accurate, or if there are other facts that were not disclosed that might cause the Department to reach a different conclusion, then the taxpayer requesting this ruling may not rely on it. A letter ruling is not equivalent to a Technical Advice Directive that generally affects a large number of taxpayers. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material aspect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that this document is not to be cited as precedent and that a change in statute, a regulation, or case law could void this ruling.

Very truly yours,

Bobby L. Weaver, Jr.

Bobby L. Weaver, Administrative Officer
Corporate, Excise, and Insurance Tax Division
TEL: (919) 733-8510
FAX: (919) 733-1821

Exhibit R

RECYCLED PAPER
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2002 WL 31153476 (Cal.St.Bd.Eq.)

State Board of Equalization
State of California

*1 IN THE MATTER OF THE APPEAL OF PACIFICORP

Not to be Cited as Precedent

Case No. 90027

September 12, 2002

Representing the Parties:
For Appellant:
Eric J. Coffill
Attorney at Law

Carley A. Roberts
Attorney at Law
For Respondent:
Craig Swieso
Tax Counsel
Counsel for Board of Equalization:

Charles D. Daly
Tax Counsel III

OPINION

This appeal is made pursuant to section 19045[FN1] of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of PacifiCorp against proposed assessments of additional franchise tax in the amounts of $498,412, $517,835, $58,523, $151,313, $359,742, and $461,972 for the years ended December 31, 1984, 1985, 1986, 1987, 1988, and 1989, respectively.

The main issue in this appeal is whether sales of electricity to California entities during the appeal years were sales of tangible personal property for purposes of section 25135. That issue is a matter of first impression in California. An alternative issue is, if the sales of electricity were sales of tangible personal property, whether the sales occurred in Oregon rather than California.

Appellant is an Oregon power company that, through its predecessor corporation Pacific Power and Light ("PPL"), has been providing electricity to the Pacific Northwest since the beginning of the previous century. Over time, PPL expanded, through the acquisition of other corporations, both the geographic areas that it served and the kinds of businesses in which it was engaged. In 1982-1985, after acquiring a large number of companies,

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PPL underwent a reorganization that apparently resulted in PPL becoming a division of appellant and appellant having primary responsibility for the management of the entire group of corporations affiliated with PPL.

The sales of the electricity at issue were made through the Pacific Northwest-Pacific Southwest Intertie ("Intertie"). The Intertie, which began operation in 1968, permits the transmission of excess power available in one region served by the Intertie to another region with power needs. Appellant states that, during the appeal years, the Intertie was owned by appellant, Portland General Electric,[FN2] and the Bonneville Power Administration ("BPA").[FN3] During most of the appeal years, the Intertie consisted of two alternating current ("AC") power lines and a direct current ("DC") power line. One AC power line ran from the Malin substation in Oregon south into California. Appellant alleges that the Western Area Power Authority[FN4] owned this line. Appellant also alleges that appellant owned the other AC power line, which ran from the Malin substation south to Round Mountain, California. In addition, appellant alleges that appellant leased that AC line to Pacific Gas and Electric ("PG&E"), Southern California Edison ("SCE"), and San Diego Gas and Electric ("SDG&E").[FN5] Finally, appellant alleges that the BPA owned the DC power line from Celilo near The Dalles, Oregon, to the Nevada-Oregon border and that the Los Angeles Department of Water and Power ("LADWP") owned that line from the Nevada-Oregon border through Nevada and into California until the line terminated in Los Angeles.[FN6]

*2 Appellant filed a California combined report with its affiliates for the appeal years.[FN7] On its Oregon corporate income tax returns for the appeal years, appellant had treated the sales of electricity to California entities as sales occurring in Oregon. Respondent's auditor in his final narrative report stated that appellant treated those sales as Oregon sales because the electricity was delivered at either the Malin substation in Oregon[FN8] or the Oregon-Nevada border and ownership of electricity sold over the Intertie changed at the contractual points of delivery. Respondent's auditor also concluded that the electricity sold to its California customers was generated by appellant and that appellant had its own generation facilities in Oregon, Washington, Montana, Wyoming, and Utah. Respondent determined upon completion of its audit that sales of electricity by appellant, doing business as PPL, to a number of power companies, municipalities, and government agencies located in California were California sales that should been included in the numerator of appellant's sales factor.[FN9]

At protest, respondent again concluded that the sales at issue were sales of tangible personal property for purposes of section 25135 and that those sales must be included in the numerator of appellant's sales factor under the then recently decided case of *McDonnell Douglas Corp. v. Franchise Tax Board* (1994) 26 Cal.App.4th 1789 ("*McDonnell Douglas*"). In *McDonnell Douglas*, the taxpayer delivered aircraft to purchasers owned by the taxpayer in California, and the purchasers then arranged for the transportation of the aircraft out of California. The court in *McDonnell Douglas* rejected the "delivery" rule adopted by respondent in its Legal Ruling 348 (Feb. 21, 1973) in favor of the "destination" rule adopted by courts in a number of jurisdictions outside of California. (*McDonnell Douglas Corp. v. Franchise Tax Board*, *supra*, 26 Cal.App.4th at pp. 1793-1796.) In respondent's view, the electricity that appellant sold was analogous to the aircraft in *McDonnell Douglas* and had an ultimate destination in California.

Subsequently, appellant petitioned respondent under section 25137 to assign appellant's sales of electricity to the locations at which the title to the electricity was contractually transferred. After respondent denied appellant's petition, this timely appeal followed.

Appellant's primary contention on appeal is that the sales of electricity at issue here are sales "other than sales of tangible personal property" for purposes of section 25136. Alternatively, appellant contends that, if the sales of electricity were sales of tangible personal property, the sales should be treated as having occurred in Oregon be-

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cause a "contractual point of delivery" rule should be adopted for electricity rather the "destination" rule announced in *McDonnell Douglas*. Appellant argues that a "contractual point of delivery" rule should be adopted for electricity because of alleged difficulties in tracing electricity from one point to another.

*3 In support of its primary contention that electricity is an "intangible,"[FN10] appellant relies heavily upon the California Supreme Court case of *Miller v. The City of Los Angeles* (1921) 185 Cal. 440 ("*Miller* ") and the California Court of Appeal case of *Pierce v. Pacific Gas & Electric Co.* (1985) 166 Cal.App.3d 68 ("*Pierce*"). In *Miller*, the issue before the Court was whether electricity was "property" for purposes of a provision of the Los Angeles City charter that permitted the purchase of "property" by the city. (*Miller v. The City of Los Angeles, supra*, 185 Cal. at pp. 443-444.) After holding that electricity was "property" for purposes of the Los Angeles city charter, the Court stated that "[e]lectricity is rather an intangible asset, and the word 'property' is perhaps not the most apt word by which to describe the supply of electrical energy thus sought to be acquired for the use of the city." (*Miller v. The City of Los Angeles, supra.*)

In *Pierce*, the appellate court considered whether electricity that injured a consumer as the result of a transformer malfunction was a "product" rather than a service for purposes of strict liability in tort. (*Pierce v. Pacific Gas & Electric Co., supra*, 166 Cal.App.3d at p. 81.) Holding that the seller of electricity was strictly liable in tort to the consumer, the appellate court in *Pierce* stated that policy justifications for imposing strict liability in tort was more significant in reaching its holding than merely whether electricity should be labeled a "product." (*Pierce v. Pacific Gas & Electric Co., supra*, 166 Cal.App.3d at p. 82.) However, after observing that California and other courts "have not dwelled unduly on electricity's physical properties" in the "product" context, the appellate court quoted in a footnote the following statement suggesting that its observation might not be entirely correct: "[b] ecause electricity is intangible, it has been consistently argued by strict liability defendants in cases involving injury by electricity that the intangible force of electric current is not a 'product' within the meaning of [[the Restatement of Torts]...,' (*Elgin Airport Inn v. Commonwealth* (1980) 88 Ill.App.3d 477 [410 N.E.2d 620,623]." (*Pierce v. Pacific Gas & Electric Co., supra*, 166 Cal.App.3d at p. 82, note 6.) Appellant also cites a number of cases from other state courts that, like *Miller* and *Pierce*, do not address the tangibility or intangibility of electricity in the context of a corporate franchise or income tax.

In further support of its position that electricity is an "intangible," appellant points out that respondent itself treated electricity as "intangible property" in its Multistate Audit Technique Manual until 1986. In addition, appellant points out that respondent has characterized electricity as an "intangible" for purposes of Public Law 86-272[FN11] in its "UDITPA Manual" (FTB Publication 1050 (Revised 10-83)) and in a letter to a commercial publisher. Appellant also notes that the Multistate Tax Commission ("MTC") considers electricity to be "intangible property" in its MTC Corporate Income Audit Procedure Guideline Manual. In addition, appellant notes that, in a 1999 report, the Federation of Tax Administrators stated that electricity should be considered a service, rather than tangible personal property, for purposes of establishing "nexus."[FN12]

*4 Appellant also cites the *Appeal of Retail Marketing Services, Inc.* (91-SBE-003), decided by the Board on August 1, 1991, for the proposition that electricity can be distinguished from "tangible personal property." In *Retail Marketing Services*, we observed that there was no statutory definition of "tangible personal property" but that the taxpayer had correctly advanced the view that "the ordinary and necessary meaning of 'tangible' is that which can be felt by touch, having actual form and substance." However, we also observed that such a definition of "tangible" is much too broad to be used in determining whether the property at issue in that matter was "tangible personal property" for purposes of the property factor under section 25129. In the matter under consideration here, appellant has provided a declaration under penalty of perjury by Richard C. Dorf, Professor of

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Electrical Engineering at the University of California at Davis, in which he concludes that "intangible personal property," under a definition allegedly consistent with *Retail Marketing Services*, encompasses electricity.[FN13] Appellant has also provided a list of cases from other states, including *Otte v. Dayton Power & Co.* (1988) 37 Ohio St. 3d 33 [523 N.E.2d 835] ("*Otte*"), to support the proposition that electricity is an "intangible" under *Retail Marketing Services*.

Finally, appellant characterizes respondent's change in position regarding the taxation of electricity as an invalid "underground regulation" whose purpose is merely to increase the collection of revenue. Appellant also expresses concern that treating electricity as tangible personal property might provide unanticipated nexus with California for companies engaged in electronic commerce.

Respondent continues to contend that electricity is tangible personal property whose sales occurred in California under the controlling authority of *McDonnell Douglas*. In support of that contention, respondent proposes a definition of "tangible personal property" as "the collective rights that are associated with things that exhibit physical attributes, which are not related to land." Respondent's proposed definition is distilled from a broad collection of sources that include dictionary definitions of "tangible personal property," a portion of a law review article[FN14] that discusses the distinction between the property law concepts of "choses in possession" and "choses in action," and respondent's apparent view that the rationale underlying the holding of *Retail Marketing Services* is that the property at issue in that matter was a "chose in action" and, therefore, was "intangible personal property." Respondent also takes the position that electricity is "tangible personal property" even under the definition of "tangible" that appellant advanced in *Retail Marketing Services*. Like appellant, respondent cites a number of cases from other jurisdictions in support of its position. However, like the cases cited by appellant, respondent's cases fail to address the tangibility or intangibility of electricity in the context of a corporate franchise or income tax.

*5 In a report submitted to us by respondent and that respondent characterizes as providing a necessary conceptual framework for discussing the scientific and technical aspects of electricity, Professor Joel Fajans, Professor of Physics at the University of California at Berkeley, states:

> "Electricity is actually a catchall word encompassing many related concepts, each with a very specific definition. These concepts include *charge*, *current* (measured in amps), *voltage* (measured in volts) *power* (measured in watts) and *energy*.... [T]he flow of charge constitutes a *current*. Charge is usually made up of electrons, so current is typically the flow of electrons.... The ability of each charge to do something useful ... is related to voltage. Thus, the rate at which electricity performs useful services equals the product of the current (the number of charges) and the voltage (the work done by each electron.) This rate is called the *power*.... [¶] .... The total amount of power consumed over time is called the energy, which is measured in kilowatt-hours. [Fn. Omitted.] ... The power company bills users for the amount of energy that they consume....
>
> The electric power distribution system is quite complicated. In essence, however, it can be reduced to a circuit consisting of a power source, a transmission line and a load.... The power source must be capable of supplying a current at a reasonable voltage, and can be, among other things, a battery, a hydroelectric plant, or a gas fired turbine generator. The transmission line can be as simple as a pair of wires like those in a household power cord. [Fn. Omitted.].... A load is the generic name for devices that use the electricity to perform a useful service."

(Resp. Br., exhibit B, p. 2.)

Later in his report, Professor Fajans further states:

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> **"Electricity is physical and material because, microscopically, it consists of the flow and 'pressure' of a material entity, namely electrons, and macroscopically, it can be sensed (felt, tasted, seen, and heard), measured, weighed, and stored, and is subject to the universal laws of nature.** The follwing sections discuss each of these properties in rough order of importance .... [¶] ... **Without electrons, electricity cannot be transmitted. Though electrons themselves are very small and lightweight, they are one of the basic constituents of matter; common matter like hydrogen and iron consists of electrons, protons, and neutrons in roughly equal number. Thus, there is nothing more physical and material than an electron. Since electricity itself consists of the flow of a material object, electricity is physical and material."**

(Resp. Br., exhibit B, p. 5.)

Respondent acknowledges that the term "other than tangible personal property" in section 25136 encompasses not only intangible personal property but also services. However, respondent argues that sales of electricity are not sales of services because electricity (1) does not essentially relate to activities conducted by individuals for the benefit of others and (2) is purchased for its "physical characteristics." From a comment in Professor Fajans' report regarding the capital required to generate and transmit electricity, respondent also argues that services performed by individuals are only incidental in comparison to generators and power lines. Other than a definition of "services" from a legal dictionary, respondent cites no authority directly in support of its arguments.

*6 With respect to the alternative issue here, respondent argues that appellant's position that the "destination" rule stated in *McDonnell Douglas* may not be applied to electricity because electricity cannot be traced from one point to another is wrong. In support of its argument, respondent points out that electricity is "fungible" and that it is irrelevant whether each electron sold by appellant can be traced to a destination in California as long as purchasers in California receive electricity equal to the amount of electricity sold by appellant. Respondent also argues that applying a "delivery" rule to electricity is inconsistent with the language in section 25135 that the f.o.b. point[FN15] or other conditions of the sale must be disregarded.

Respondent concedes that if the sales of electricity at issue are sales of "other than tangible personal property" for purposes of section 25136, the sales were not in California under that section because a majority of the "income-producing activities" related to those sales were performed in other states, based on cost of performance.

Section 25128 provides that all business income shall be apportioned to California by multiplying such income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is three. Section 25134 defines the sales factor as a fraction, the numerator of which is the total number of sales of the taxpayer in California during the income year, and the denominator of which is the total sales of the taxpayer everywhere during the income year.

Section 25135 provides that sales of tangible personal property are in California if: (a) the property is delivered or shipped to a purchaser, other than the United States Government, within California regardless of the f.o.b. point or other conditions of the sale; or (b) the property is shipped from an office, store, warehouse, factory, or other place of storage in California and (1) the purchaser is the United States government or (2) the taxpayer is not taxable in the state of the purchaser. Section 25136 provides that sales, other than sales of tangible personal property, are in California if: (a) the income-producing activity is performed in California; or (b) the income-producing activity is performed both in and outside California and a greater proportion of the income-producing

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activities is performed in California than in any other state, based on costs of performance.

California Code of Regulations, title 18, section 25136, subdivision (b), ("Regulation section 25136, subdivision (b)") provides as follows:

"The term 'income producing activity' applies to each separate item of income and means the transactions and activity directly engaged in by the taxpayer in the regular course of its trade or business for the ultimate purpose of obtaining gains or profit. Such activity does not include transactions and activities performed on behalf of a taxpayer, such as those conducted on its behalf by an independent contractor. Accordingly, income producing activity includes but is not limited to the following:

*7 1. The rendering of personal services by employees or the utilization of tangible and intangible property by the taxpayer in performing a service.

2. The sale, rental, leasing, licensing, or other use of real property.

3. The rental, leasing, licensing or other use of tangible personal property.

4. The sale, licensing or other use of intangible personal property.

"The mere holding of intangible personal property is not, of itself, an income producing activity."

We agree with appellant's primary contention that the sales of electricity here are "other than sales of tangible personal property" for purposes of section 25136. Because their discussions of the tangibility or intangibility of electricity are not in the context of a corporate franchise or income tax and are sometimes, as in *Miller* and *Pierce*, mere dictum, the cases and other authority upon which appellant relies are not controlling here. However, discussions of electricity in some of those cases are nonetheless helpful in resolving the main issue in the instant matter. For example, in the *Otte* case cited by appellant, the Ohio Supreme Court distinguished electricity from a "product" in the context of strict liability in tort by stating as follows:

"A 'product' is anything made by human industry or art. electricity appears to fall outside this definition. This is so because electricity is the flow of electrically charged particles along a conductor. [The power company] does not manufacture electrically charged particles, but rather, sets in motion the necessary elements that allow the flow of electricity. What we have here is a purported defect in the distribution system. Such a system is, in our view, a service."

(*Otte v. Dayton Power & Co.*, *supra*, 37 Ohio St. 3d at p. 37.)

Like the court in *Otte*, we conclude that the sales of electricity here are sales of services that essentially consisted of appellant's setting and keeping in motion, through its generation and transmission facilities, electrically charged particles. Also as in *Otte*, we further conclude that the basic reason the generation and transmission process employed by appellant is appropriately characterized as a service is that the process does not result in either (1) the "creation" in its generation facilities of any such arguably tangible particles or (2) the "injection" of those particles into its transmission facilities.

At this juncture in our analysis, it is necessary to point out that exactly what constitutes the "sales of electricity" at issue here is not well specified in the record. For example, appellant has not presented us with financial or other records that segregate its "sales of electricity" to California entities into such components as sales resulting from the generation of electricity and sales resulting from the transmission of electricity. However, the final narrative report of respondent's auditor notes that when a California entity purchases "power" from appellant, appellant "turns up" its generator to put more power into the Intertie. In addition, the auditor's report notes that there were "wheeling" charges for transmitting electricity over power lines. In view of the auditor's notations, we infer that the generation and transmission of electricity by appellant are the components of the "sales of electricity" that we need to consider here. The auditor's report also states that a California entity would pay a "use of

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facilities" charge to use power lines owned by another entity. However, as indicated in footnote 5, it appears that rental payments for the California portion of those lines are not at issue here because appellant has already included them in the numerator of its sales factor under Regulation section 25136, subdivision (b)(2).

*8 Even though respondent seems to argue that the generation and transmission of electricity are not properly treated as services under section 25136 because they are not personal services, Regulation section 25136, subdivision (b)(1), explicitly states that "income producing activity" is not limited to personal services by employees but includes the use of tangible and intangible property in performing a service. In addition, we concluded in the *Appeal of Mark IV Metal Products, Inc.* (82-SBE-181), decided by the Board on August 17, 1982, that the fabrication in California of metal owned by a Texas customer into seat parts for that customer, through the use of the taxpayer's "own labor and machinery," was a service that was includable in the numerator of a taxpayer's sales factor under section 25136. For those reasons, we reject respondent's argument that the generation and transmission of electricity are not properly treated as services under section 25136 because they are not personal services.

Respondent appears to predicate its argument that electricity is not a service because it is purchased for its "physical characteristics" on the assumption that the generation and transmission of electricity are inseparable from, and incidental to, its "physical characteristics." However, as suggested by *Otte*, the "physical characteristics" of electricity in the instant matter are essentially the electrons already in the power lines that have been set and kept in motion by appellant's generation and transmission system.[FN16] Because appellant has apparently already paid for the use of the electrons in the power lines by payment of the "use of facilities" charge in transactions that are separate from, and independent of, those regarding the generation and transmission of electricity, we conclude that the generation and transmission of electricity here are neither inseparable from, nor incidental to, its "physical characteristics." Because we disagree with respondent's underlying assumption, we also disagree with its argument that electricity is not a service because it is purchased for its "physical characteristics."

With regard to respondent's argument that the services performed by appellant in the generation and transmission of electricity were merely incidental in comparison to generators, *Mark IV Metal Products* clearly supports the view that the use of equipment, such as a generator, by a taxpayer as part of the process by which a service is performed does not detract from the conclusion that the taxpayer is performing a service for purposes of section 25136. As discussed above, respondent's argument that the generation and transmission of electricity were merely incidental in comparison to power lines also fails because the rentals of the power lines are transactions that are separate from, and independent of, those relating to the generation and transmission of the electricity.

Although Professor Fajan's discussion of electricity in his report seems intended to support respondent's position that electricity is "tangible personal property" by emphasizing the "physical and material" nature of electrons, his discussion is also consistent with the definition of electricity in *Otte* as a "flow of electrically charged particles along a conductor." In addition, Professor Fajan's discussion of electricity is also consistent with the conclusion of the court in *Otte* that the "distribution system" with respect to electricity there was a service. In our view, just as the "distribution system" by which the flow of electrically charged particles occurred in *Otte* was a service, appellant's generation and transmission of electricity were also services under section 25136.

*9 Because we conclude that sales of the generation and transmission of electricity here were sales of services performed for the most part outside of California, we further conclude that those sales were sales of "other than tangible personal property" and were properly excluded from the numerator of appellant's sales factor. Therefore, based upon the foregoing discussion, we conclude that, for purposes of California tax law, electricity is in-

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tangible. In view of our conclusions, we need not address the alternative issue in this matter.

Accordingly, respondent's action is hereby reversed.

ORDER

Pursuant to the views expressed in the opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED, AND DECREED, pursuant to section 19047 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of PacifiCorp against proposed assessments of additional franchise tax in the amounts of $498,412, $517,835, $58,523, $151,313, $359,742, and $461,972 for the years ended December 31, 1984, 1985, 1986, 1987, 1988, and 1989, respectively, be and the same is hereby reversed.

Done at Sacramento, California, this 12 day of September, 2002, by the State Board of Equalization, with Board Members Dean Andal, Claude Parrish and *Marcy Jo Mandel present.

FN1. Unless otherwise specified, all section references are to sections of the Revenue and Taxation Code as in effect for the years in issue.

FN2. Portland General Electric is an Oregon subsidiary of Enron Corporation.

FN3. The BPA is an agency of the United States government. Apparently, a major purpose of Congress in authorizing the construction of the Intertie was to provide an additional market for surplus power provided by the BPA so that the BPA would have greater financial resources to repay the United States Treasury for its investment in the Pacific Northwest power system.

FN4. We assume that the "Western Area Power Authority" is the same entity as the entity designated as WAPA in footnote 9.

FN5. Apparently, appellant included rental income from the portion of the line that ran from the Oregon-California border to Round Mountain, California, in the numerator of its sales factor. Appellant's treatment of that rental income does not seem to be in dispute.

FN6. We note that appellant does not attempt to reconcile seeming inconsistencies between its statement that appellant, Portland General Electric, and the BPA were co-owners of the Intertie with its allegations regarding the ownership of the AC and DC power lines that comprised the Intertie. However, we also note that respondent does not seem to object to such inconsistencies. Therefore, we conclude that they are of little significance here.

FN7. At protest, respondent determined that appellant was unitary, and therefore should be combined, with only some of the affiliates that were included in its California combined report.

FN8. The audit report also stated that some of appellant's contracts with its California purchasers provided that the sales of electricity would occur at the Oregon-California border because of the possibility that an additional AC power line would be constructed that would not pass through the Malin substation.

FN9. Of appellant's sales of electricity to the California entities during the appeal years, approximately 47 per-

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cent ($224,919,960) were made to SCE, 20 percent ($92,765,217) to PG&E, 18 percent ($85,684,193) to LADWP, Sacramento Municipal Utility District, and various California municipalities, and 14 percent ($66,209,039) to the California Department of Water Resources. Appellant also made sales of electricity of $4,237,171 to SDG&E during the appeal years and of $16,036,408 to the Western Area Power Administration ("WAPA") during the 1984-1986 appeal years. Because respondent apparently has concluded that the sales to WAPA may have been, in effect, sales to purchasers that were not located in California, respondent concedes that those sales should not be included in the numerator of appellant's sales factor. The record contains no additional information regarding the functions of WAPA or its constituent parts.

FN10. Like respondent, appellant sometimes uses the term "an intangible" or other similar designation as synonymous with the term "other than sales of tangible personal property" under section 25136.

FN11. Public Law 86-272 provides, in pertinent part, that no state shall have the power to impose a net income tax on income derived within the state if the only business activity within the state is the solicitation of orders for sale of tangible personal property, which orders are sent outside the state for approval or rejection and, if approved, are filled by shipment or delivery from a point outside the state. (15 U.S.C.A., § 381(a)(1).)

FN12. "Nexus," in this context, is another way of saying that a corporate taxpayer has sufficient connections with a state to justify, for constitutional purposes, taxation of the taxpayer by that state.

FN13. Professor Dorf's testimony at the hearing in this matter was to the same effect.

FN14. Cowdrey, *Software and Sales Taxes: The Illusory Intangible* (1983) 63 B.U. L.Review 181, 197-209.

FN15. With regard to the term "f.o.b. point," California Commercial Code section 2319 (1) provides, in pertinent part, that "(a) [w]hen the [delivery] term is F.O.B. [an abbreviation for "free on board"] the place of shipment, the seller must at that place ship the goods in the manner provided in this division (Section 2504) and bear the expense and risk of putting them in the possession of the carrier; or (b) [w]hen the term is F.O.B. the place of destination, the seller must at his own expense and risk transport the goods to that place and there tender delivery of them in the manner provided in this division Section 2503."

FN16. For a more complete discussion of the generation of electricity in modern power plants, see Serway, Physics for Scientists and Engineers with Modern Physics (1990), pp. 886-888.

2002 WL 31153476 (Cal.St.Bd.Eq.)

END OF DOCUMENT

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Exhibit S

RECYCLE PAPER
RECYCABLE

2006 WL 1085380 (Mass.App.Tax.Bd.)

Appellate Tax Board
Commonwealth of Massachusetts

EUA OCEAN STATE CORPORATION, ET AL.
[FN1]

v.

COMMISSIONER OF REVENUE

Docket Nos.
C258405-406, C258424-425, C258882-883, C259158-159, C259653 and C262566-568

April 24, 2006

These are appeals under the formal procedure pursuant to G.L. c. 58A, § 7 and G.L. c. 62C, § 39, from the refusal of the appellee Commissioner of Revenue ("Commissioner") to abate corporate excises assessed against appellants under G.L. c. 62C, § 26 and G.L. c. 63, §§ 32 and 39, for tax years ranging from 1994 through 1998.

Commissioner Scharaffa heard these appeals and was joined in the decision for appellants by Commissioners Gorton, Egan, and Rose. Chairman Foley took no part in the deliberation or decision of these appeals.

These findings of fact and report are promulgated at the request of both appellants and the Commissioner pursuant to G.L. c. 58A, § 13 and 831 CMR 1.32.

John S. Brown, Esq., Joseph L. Kociubes, Esq., George P. Mair, Esq., Donald-Bruce Abrams, Esq., Darcy A. Ryding, Esq., and *Matthew D. Schnall, Esq.*
for the appellants.

Daniel A. Shapiro, Esq., and *Thomas W. Hammond, Esq.*,
for the appellee.

FINDINGS OF FACT AND REPORT

I. INTRODUCTION

*1 On the basis of the parties' Statement of Agreed Facts, the testimony of witnesses at the two-day hearing before the Appellate Tax Board ("Board"), and documents submitted at the hearing, the Board made the following findings of fact.

Appellants EUA Ocean State Corporation ("EUA"), National Grid USA Service Company, Inc. ("National Grid"), TCPL OSP Ltd. ("TCPL OSP"), TCPL OSL Ltd. ("TCPL OSL"), and TCPL Power Ltd. ("TCPL Power") appeal from the refusal of the Commissioner to abate approximately $1.3 million in corporate excises assessed against them for various tax periods between 1994 and 1998.[FN2] Appellants are partners in two Rhode Island general partnerships, Ocean State Power ("OSP") and Ocean State Power II ("OSP II" and, togeth-

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er with OSP, the "Partnerships"), that generated and sold electricity during the periods at issue.

The principal issue raised in these appeals is whether any of the Partnerships' sales of electricity should be treated as Massachusetts sales includible in the numerator of appellants' sales factors under G.L. c. 63, § 38(f). [FN3] If, as the Commissioner maintains, electricity is tangible personal property, the sales are considered to have occurred in the state where title and possession of the electricity passed and appellants' sales factors would include their Massachusetts sales in the numerator and all electricity sales in the denominator. If, however, electricity is not tangible personal property, the sales are attributed to the state in which appellants incurred the greatest proportion of the costs of performing their income-producing activity. It is not disputed that under the non-tangible property attribution rule, all of the Partnerships' sales would be attributed to Rhode Island and not Massachusetts because they incurred all of their costs of performance in Rhode Island.

On their Massachusetts corporate excise returns, appellants did not report any of the Partnerships' sales of electricity as Massachusetts sales includible in the numerator of their sales factors. On audit, however, the Commissioner treated more than seventy-five percent of those sales as Massachusetts sales.

II. IDENTIFICATION OF APPELLANTS AND JURISDICTION

A. EUA

EUA is a Rhode Island corporation that was formed as a special purpose subsidiary of Eastern Utility Associates for the purpose of being a partner in the Partnerships. EUA was a general partner in the Partnerships and held a twenty-nine percent interest in each of the Partnerships throughout the period from 1994 through 1998. EUA's sole business activity during this time was to act as a general partner in the Partnerships.

As a result of his adjustments to the Partnerships' sales factors, the Commissioner made additional assessments against EUA with respect to both the net income and the net worth components of its corporate excise for each of the tax years 1994 through 1998. EUA is contesting approximately $355,000 of additional assessments for these periods. On the basis of the Statement of Agreed Facts and accompanying exhibits, the Board found that EUA timely filed its returns, Applications for Abatement, and petitions for the tax years at issue. Accordingly, the Board found and ruled that it had jurisdiction over EUA's appeals (Docket Numbers C258406, C259159, and C259653).

B. TCPL OSP/NERC

*2 TCPL OSP is a Rhode Island corporation that was formed as a special purpose subsidiary of New England Electric System for the purpose of being a partner in the Partnerships. TCPL OSP was a general partner in each of the Partnerships and held a twenty percent interest in each of the Partnerships during 1994 and throughout the period from 1996 through 1998. During those periods, TCPL OSP's sole business activity was to act as a general partner of the Partnerships. TCPL OSP was formerly known as Narragansett Energy Resources Company ("NERC").

As a result of his adjustments to the Partnerships' sales factors, the Commissioner made additional assessments against TCPL/NERC with respect to the net worth component of its corporate excise for the tax years 1994, 1996, and 1997. In addition, the Commissioner made assessments against TCPL OSP with respect to both the net worth and net income components of its corporate excise for the portion of the 1998 taxable year for which TCPL OSP filed a separate return (September 2 through December 31, 1998). TCPL OSP is contesting approximately $36,000 in additional assessments for these periods. On the basis of the Statement of Agreed Facts and accompanying exhibits, the Board found that TCPL OSP/NERC timely filed its returns, Applications for Abate-

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ment, and petitions for the tax years at issue. Accordingly, the Board found and ruled that it had jurisdiction over TCPL OSP/NERC's appeals (Docket Numbers C258424, C258882, and C262568).

C. NATIONAL GRID/NEPSC

During 1994 and the period from January 1, 1997 through September 1, 1998, National Grid, then known as New England Power Service Company ("NEPSC"), was the principal reporting corporation for an affiliated group that included TCPL OSP. National Grid is a party to this appeal solely as the principal reporting corporation for this affiliated group.

For tax year 1994, TCPL OSP, then known as NERC, was part of the affiliated group for which NEPSC filed a combined return. NERC's income was included in computing the tax assessed against NEPSC with respect to the group's combined net income pursuant to G.L. c. 63, § 32B. As a result of his adjustments to the Partnerships' sales factors and adjustments to the income of another member of the group, the Commissioner made an additional assessment of $65,784 against NEPSC with respect to the combined net income for tax year 1994. The parties agree that, as a result of the Board's decision in **New England Power Service Co. v. Commissioner of Revenue**, ATB Findings of Fact and Reports 2000-56, National Grid/NEPSC is entitled to an abatement of $65,784 for 1994, regardless of the resolution of the contested issue regarding the Partnerships' sales factors and the treatment of NERC as a business corporation rather than a utility corporation.

On the basis of the Statement of Agreed Facts and accompanying exhibits, together with the Commissioner's concession at the hearing that NEPSC had not received a Notice of Abatement Determination dated June 7, 2000 until after it had filed its petition, the Board found that NEPSC timely filed its return, Application for Abatement, and petition for tax year 1994. Accordingly, the Board found and ruled that it had jurisdiction over NEPSC's 1994 appeal (Docket Number C258405).

*3 During the period from January 1, 1997 through September 1, 1998, NERC was also part of the affiliated group for which NEPSC filed a combined return pursuant to § 32B for tax years 1997 and 1998. As a result of his adjustments to the Partnerships' sales factors, the Commissioner reduced the amount of refund that he determined to be due to NEPSC for tax year 1997 and made an additional assessment against NEPSC with respect to NERC's income for tax year 1998.

National Grid/NEPSC is contesting approximately $105,000 in additional assessments for tax years 1997 and 1998. On the basis of the Statement of Agreed Facts and accompanying exhibits, the Board found that National Grid/NEPSC timely filed its returns, Applications for Abatement, and petitions for the tax years 1997 and 1998. Accordingly, the Board found and ruled that it had jurisdiction over National Grid/NEPSC's 1997 and 1998 appeal (Docket Number C262566).

D. TCPL OSL

TCPL OSL is a Rhode Island corporation that was formed for the purpose of being a partner in the Partnerships. TCPL OSL was a general partner in each of the Partnerships and held a ten and one-tenth percent interest in each of the Partnerships during 1994 and throughout 1997 through 1998. During those periods, TCPL OSL's sole business activity was to act as a general partner of the Partnerships. TCPL OSL was formerly known as JMC Ocean State Corporation.

As a result of his adjustments to the Partnerships' sales factors, the Commissioner made additional assessments against TCPL OSL with respect to the net worth component of its corporate excise for tax year 1997. In addition, the Commissioner made assessments against TCPL OSL with respect to both the net worth and net income

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components of its corporate excise for the portion of the 1998 taxable year for which TCPL OSL filed a separate return (July 3 through December 31). TCPL OSL is contesting approximately $14,500 in additional assessments for the tax years 1997 and 1998. On the basis of the Statement of Agreed Facts and accompanying exhibits, the Board found that TCPL OSL timely filed its returns, Applications for Abatement, and petitions for tax years 1997 and 1998. Accordingly, the Board found and ruled that it had jurisdiction over TCPL OSL's appeals (Docket Numbers C259158 and C262567).

E. TCPL POWER

Like EUA, TCPL OSP, and TCPL OSL, TCPL Power is a Rhode Island corporation that was formed for the purpose of being a partner in the Partnerships. TCPL Power was a general partner in each of the Partnerships and held a forty percent interest in each of the Partnerships during the tax years 1994 through 1998. During those years, TCPL Power's sole business activity was to act as a general partner of the Partnerships.

As a result of his adjustments to the Partnerships' sales factors, the Commissioner made additional assessments against TCPL Power with respect to both the net worth and net income components of its corporate excise for each of the tax years 1994 through 1998. TCPL Power is contesting approximately $670,000 in additional assessments for these periods. On the basis of the Statement of Agreed Facts and accompanying exhibits, the Board found that TCPL Power timely filed its returns, Applications for Abatement, and petitions for the years at issue. Accordingly, the Board found and ruled that it had jurisdiction over TCPL Power's appeals (Docket Numbers C258425 and C258883).

III. THE PARTNERSHIPS' BUSINESS ACTIVITIES

*4 At all material times, each of the Partnerships owned and operated an electric generating plant in Burrillville, Rhode Island, near the Massachusetts border (the "Plants"). OSP owned and operated an approximately 249 megawatt, natural-gas fired, combined-cycle electric generating plant that included two General Electric MS-7000 EA gas turbines and one General Electric condensing steam turbine-generator ("Unit I"). OSP II owned and operated an approximately 243 megawatt, natural-gas fired, combined-cycle generating plant that, like Unit I, also included two General Electric MS-7000 EA gas turbines and one General Electric condensing steam turbine-generator ("Unit II" and, together with Unit I, the "Units"). The Partnerships derived the bulk of their revenue, roughly $100 million per year for each Partnership, from the sale of electricity generated by the Units and the sale of "capacity," the right to purchase a portion of the electricity that the Units could generate.

The Partnerships also sold excess natural gas during periods when the Units were not operating. Revenues from these natural-gas sales ranged from $800,000 to nearly $10 million per year during the periods at issue. The Partnerships sold no natural gas to Massachusetts customers.

The Partnerships owned various residential properties in Massachusetts and Rhode Island that were located within a half-mile radius of the Plants. The Partnerships purchased these properties from their prior owners under a so-called "property value stabilization program." The program was instituted as part of the process by which the Partnerships gained the necessary governmental approvals for constructing the Plants in response to objections from owners who did not want to have the Plants located near their homes. During the periods at issue, the Partnerships either sold the residential properties to new owners or leased the properties. The Partnerships did not use the properties in the operation of the Plants. As the Partnerships sold the residential properties during the periods at issue, revenues decreased from $87,286 in 1994 to $25,033 in 1998.

The assessments at issue concern only the Partnerships' sale of electricity. The Commissioner made no adjust-

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ments concerning receipts from the Partnerships' Massachusetts real estate or the sale of "capacity" and natural gas.

IV. COMMISSIONER'S ALLOCATION OF SALES TO MASSACHUSETTS

For the majority of the tax years at issue, the utilities purchasing electricity from the Partnerships were: Boston Edison Company ("BECO"); Montaup Electric Company ("Montaup"); and New England Power Company ("NEP") (together, "Purchasers"). TransCanada Power Marketing Ltd. ("TCPM") replaced both Montaup and NEP as a purchaser during the end of the periods at issue. [FN4] During the tax years at issue, the Purchasers were engaged in the wholesale and/or retail sale of electricity.

One of the Purchasers, BECO, was primarily engaged in the retail sale of electricity in Massachusetts. However, over ten percent of BECO's sales were sales to other electricity distributors for resale. These distributors included utilities located in other New England states and power marketing and trading companies that operated throughout the United States.

*5 Another purchaser, NEP, was engaged almost exclusively in the wholesale transmission and resale of electricity, including sales to affiliates based in Massachusetts (Massachusetts Electric Company), Rhode Island (The Narragansett Electric Company), and New Hampshire (Granite State Electric Company). NEP also sold power to unaffiliated customers during the years at issue, including power companies and municipal light departments in various states, and marketing and trading companies selling power throughout the United States. NEP also entered into system power contracts in which it sold specified quantities of power during specific periods to other wholesalers and unit power contracts in which it sold specified quantities of power.

NEP also transferred a portion of its right and obligation to purchase electricity from the Partnerships during the periods at issue. NEP transferred between two and eight percent of the total output of the Partnerships' Units during the period at issue to Unitil Power Corporation ("Unitil"), a New Hampshire utility.

A third purchaser, Montaup, was engaged primarily in the wholesale transmission of power. Montaup's customers included NEP, BECO, and Montaup's affiliates, Eastern Edison Company (based in Massachusetts), BE (based in Rhode Island), and Newport Electric Company (also based in Rhode Island). Its other customers included utilities based in Massachusetts, Rhode Island, Connecticut, a Rhode Island municipal light district, and trading companies doing business throughout New England.

The Commissioner audited appellants' Massachusetts corporate excise returns and determined that appellants' treatment of all electricity sales as non-Massachusetts sales was in error. The auditor initially treated all sales of electricity and capacity as sales of tangible personal property and relied on the "reverse dock sale rule" found in 830 CMR 63.38.1(9)(c) to treat these sales as Massachusetts sales because the electricity was "transshipped" from Rhode Island to Massachusetts customers via the "common carrier" of the New England electricity distribution system known as the "NEPOOL grid," which is described in Section V(B) below. Because for most of the tax years at issue, the Purchasers were all based in Massachusetts, the auditor assumed that the destination of all the Partnerships' sales of electricity during that period was Massachusetts.

Appellants appealed this determination to the Department of Revenue's Appeal and Review Bureau ("A&R"). A&R revised the auditor's determination and concluded that it was the location of the "residential, commercial, and industrial end-users" of the electricity, and not the location of the "intervening purchaser or supplier," that determined whether the sale was a Massachusetts sale. Accordingly, A&R determined that sales of electricity were includible in the numerator of appellants' sales factors "to the extent that the electricity [was] consumed

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and used by the Purchasers' ultimate retail customers in Massachusetts."

*6 The auditor then prepared a revised set of workpapers based on his understanding of the A&R decision. To determine the identity of the Purchasers' customers, the auditor reviewed certain filings made by the Purchasers to the Federal Energy Regulatory Commission ("FERC"). He then made assumptions, based on the name of the customer or other information he was told, concerning the locations of the ultimate retail consumers of the electricity.

For example, the auditor treated all sales to Massachusetts Electric, but no sales to Narraganset Electric, as Massachusetts sales, solely based on their names. Similarly, he treated all sales to Eastern Edison, but no sales to Granite State Electric, as Massachusetts sales, because he was told that "Eastern Edison was 100 percent Mass." and that Granite State "does business in New Hampshire."

He did not attempt to determine the identity or location of the retail customers of those entities that purchased electricity from the Purchasers. Rather, he used an "all-or-nothing" approach, classifying either all, or none, of the sales made by the Purchasers' customers as Massachusetts sales strictly based on the name of the Purchasers' customer or other information relayed to him. For example, all of BECO's sales were considered to be Massachusetts sales because the auditor "assumed [BECO] was 100 percent Mass.," even though the A&R determination acknowledged that BECO "did make some wholesale sales to other utilities such as EUA's parent, Eastern Utility Associates, which conducts a substantial portion of its operations in Rhode Island."

To determine the percentage of the Partnerships' total electricity sales attributable to Massachusetts, the auditor first determined the Partnerships' total electricity sales to each purchaser, and then computed a "Massachusetts Sales Percentage" that he applied to the Partnerships' electricity sales to each purchaser. The auditor arrived at the Massachusetts Sales Percentage by dividing what he determined to be each purchaser's sales to Massachusetts customers by the Purchasers' total sales.

Using 1994 as an example, the auditor first broke down the Partnerships' total electricity sales of $30,245,388 among Montaup ($11,009,196), NEP ($19,069,501) and BECO ($9,239,861). For Montaup, he derived a Massachusetts Sales Percentage of 61.9012 percent from an excerpted page from Montaup's 1994 FERC filings. He arrived at this percentage by first treating all $41,466,446 of Montaup's sales to Eastern Edison Company as Massachusetts sales. He then added the Eastern Edison sales to $20,423,209 of sales to Blackstone Valley Electric and $5,109,429 of sales to Newport Electric to arrive at a total sales figure of $66,988,084. The Massachusetts Sales Percentage of 61.9012 percent is equal to the Eastern Edison Sales divided by the sum of the Eastern Edison, Blackstone Valley Electric, and Newport Electric sales. The auditor disregarded all other Montaup sales, including all sales to non-affiliates.

*7 The auditor used a similar approach to arrive at a Massachusetts Sales Percentage of 74.4157 percent for NEP for 1994. He treated all of NEP's sales to Massachusetts Electric, totaling $357,642,672, as Massachusetts sales. He then treated $16,044,384 in sales to Granite State Electric and $106,914,299 in sales to Narragansett Electric as non-Massachusetts sales. Dividing the sales to Massachusetts Electric by all NEP sales, he arrived at the 74.4157 Massachusetts Sales Percentage for NEP.

For BECO, the auditor assumed that all of BECO's electricity sales were to Massachusetts customers. Accordingly, he used a Massachusetts Sales Percentage of one hundred percent.

The auditor then determined the Massachusetts sales for each of the Partnerships by multiplying the Partner-

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ships' sales to each purchaser by the Massachusetts Sales Percentage that he had calculated for each of the Purchasers, adding the results together, and allocating the total between the two Partnerships. He then adjusted the apportionment formulas for each of the partners by adding the amounts he determined to be Massachusetts sales to the numerator of the sales factor.

The auditor acknowledged that there were difficulties in applying the methodology described in the A&R Determination letter. First, the Partnerships could not tell from their own records the location of "the ultimate retail customers" as required by the A&R Determination Letter. Moreover, because NEP's and Montaup's customers were also engaged in the transmission, distribution and wholesaling of electricity, and were therefore not the "ultimate consumers" of the electricity purchased, the FERC filings made by NEP and Montaup could not establish the location of the ultimate consumers because these records would not show whether a transmission or distribution purchaser located outside of Massachusetts resold electricity back into Massachusetts or vice versa.

Further, although it does not appear to be a relevant factor for applying the A&R method, the auditor also testified that the Massachusetts "headquarters" of the Purchasers also supported the assessment. The auditor testified that because the three principal Purchasers - BECO, Montaup, and NEP - were all "headquartered" in Massachusetts and headquarters is where the "retail obligation is," the actual "possession and control" of the electricity sold to them passes in Massachusetts.

The Commissioner's allocation of electricity sales to Massachusetts and the resulting assessments against appellants are premised on his determination that sales of electricity are "sales of tangible personal property" for purposes of G.L. c. 63, § 38(f). Accordingly, the Board found the following facts concerning the Partnerships' generation, distribution, and sale of electricity to determine whether electricity constitutes "tangible personal property."

V. PARTNERSHIPS' GENERATION AND SALE OF ELECTRICITY

A. GENERATION OF ELECTRICITY

*8 Electricity is produced at each Unit using two 80-megawatt natural gas generators and one 90 megawatt steam generator. The generation process begins with the activation of two natural gas turbines, which are similar to aircraft jet engines. The combustion of natural gas causes the rotor in each turbine to rotate at very high speed. The heat exhaust from the gas turbines is used, in conjunction with the burning of additional fuel, to heat water to produce steam. The steam is used as the power source for the steam turbine, causing the rotor in the steam turbine to rotate.

Each generator consists of a "stator" and a "rotor." The stator is a series of stationary coils around the periphery of the generator. Inside the stator is the rotor winding, a coil connected to the turbine that produces a magnetic field. The high-speed rotation of the rotor within the stator causes a changing magnetic field. The changing magnetic field induces a flow of current, or electricity, in the stator.

No new electrons or other "particles" are created by this process. The changing magnetic field caused by the rotation of the rotor causes electrons in the stator coils to move in alternating directions, resulting in "alternating current." In the United States, the standard current used is 60-cycle current, in which there are 60 alternating cycles per second, referred to as "60 hertz" or "60 HZ." In 60 hertz current, electrons change direction 120 times per second.

The rapid oscillation of electrons caused by the rotation of the rotor within the stator results in a flow of energy

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within the coils of the stator. The electrons themselves do not flow in any one direction; for example, individual electrons do not flow out of the generator, onto the transmission lines and into consumers' homes and businesses. Rather, the oscillation of the electrons within the stator of the generator causes a flow of electrical energy which, as described below, is distributed to electricity consumers.

B. TRANSMISSION AND DISTRIBUTION OF ELECTRICITY

The electrical energy flows out of the stator on wires to a transmission substation where the energy generated at the Units is transferred to the transmission system servicing New England, known as the New England Power Pool ("NEPOOL") transmission grid (the "grid"). The grid is a series of interconnected transmission lines throughout New England carrying power generated by the Partnerships and by other generating facilities to delivery points for distribution to New England consumers. The grid consists of that portion of the distribution system between "transmission substations," located near generating facilities, and "power substations," located near the consumer. NEPOOL is not involved in the delivery of power from generation facilities to the transmission substation or the distribution of the power from the power substation to the consumer.

The substation at which the electricity generated by the Units is transferred to the grid is called the "Sherman Farm Road Extra High Voltage/Pool Transmission Facility" ("EHV/PTF"). The EHV/PTF is also located in Rhode Island, a few hundred feet from the Plants. It is owned by Blackstone Valley Electric Company.

*9 Efficient distribution of electrical energy over wires requires a voltage, which is the measure of the energy's force, of 345 kilovolts ("KV"). The voltage of the power produced by the Units' generators is typically only 13 to 20 KV. Therefore, the power flowing from the generators is put through a series of "transformers" before it is transferred to the grid at the EHV/PTF. A transformer consists of two coils of wires, called "windings," that are wrapped around a magnetic core. Current flowing through one winding at a given voltage induces a magnetic field in the core, which in turn induces a current at a different voltage in the other winding. There is no physical connection or movement of electrons between the two windings; the only connection is through a magnetic field.

Once its voltage reaches the proper level, the electricity is "impressed" or "injected" onto the grid for distribution throughout New England. Electricity is distributed through an integrated system of transmission and distribution facilities using interconnected transmission lines, transformers, and other equipment to bring the power generated by the Partnerships and other power generators to consumers. Just as the voltage is stepped up at transmission substations such as the EHV/PTF to efficiently travel over wires, it must be stepped down to be usable by customers. Generally, the voltage is first reduced to an intermediate level suitable for bringing the electricity into various distribution areas, then reduced further at power substations to an appropriate distribution voltage level, and then, at or near the customer, the voltage is further reduced to a level suitable for customer use. The voltage reduction is achieved using transformers, which operate in the same general manner as the transformers used to increase its voltage.

C. CONTRACTS REGARDING THE SUPPLY OF ELECTRICITY

1. NEPOOL

NEPOOL is an organization of electric utilities created by the NEPOOL Agreement. NEPOOL was formed as a result of the unprecedented power blackout that occurred in New York and New England in 1965. The goals of NEPOOL are to maintain the reliability of the bulk power system for the delivery of electricity to consumers and to produce and deliver power at the lowest cost that is consistent with prudent utility practice.

The NEPOOL Agreement is a contractual agreement among electric utilities that is open to all electric utilities

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operating in New England. During the tax years at issue, the Purchasers were members of NEPOOL, but the Partnerships were not. The NEPOOL Agreement provides the central dispatching and primary pooling arrangement for electric utilities operating in New England.

(a) SCHEDULING OF POWER GENERATION

NEPOOL does not own any generating or transmission facilities. Rather, it or its agents schedule the operation of the generation facilities that contribute to the NEPOOL grid, including the Partnerships' Units, and account for the purchases and sales of electricity among its members.

*10 Although NEPOOL is not directly involved in the physical operation of the generating plants, it does determine the output levels at which the plants operate. The output levels are based on a projection that takes into account the amount of power withdrawn from the grid by power purchasers and anticipated "line losses," the dissipation of electricity during the transmission process resulting from the inherent resistance of conductors. During most of the periods at issue, decisions concerning the plants' output levels were made by NEPOOL's dispatch agent, the New England Power Exchange, or NEPEX.

(b) SETTLING ACCOUNTS AMONG MEMBERS

During the tax years at issue, the Partnerships sold all of the electricity they produced at the Plants to the Purchasers, who were engaged in the transmission and/or distribution of electricity.

Each of the Purchasers entered into a Unit Power Agreement with each of the Partnerships governing the sale of electricity to that purchaser. Under the Unit Power Agreement, the Partnerships were obligated to sell, and the Purchasers were obligated to purchase, the following percentages of the Partnership's output: BECO, twenty-three and one-half percent; Montaup, twenty-eight percent; NEP, forty-eight and one-half percent.

NEPOOL accounted for the activity of its members in terms of "resources" and "loads." Resources are the amount of power that a NEPOOL member contributed to the grid and "loads" are the amount of power that a member withdrew from the grid. For example, power generated and transferred to the grid by the Partnerships would be credited as resources to each of the Purchasers in proportion to the percentage of power that the purchaser was entitled and obligated to purchase. Conversely, each of the Purchasers would be charged with loads when its wholesale or retail customer withdrew power from the grid. A deficit in resources in effect represented a purchase by the NEPOOL member from other members, while an excess of resources over loads in effect represented a sale into the pool.

NEPOOL and its administrative agents determined on an hourly basis the net amount of each NEPOOL member's resources and loads. The net purchases and sales were then settled on a monthly basis as a net dollar amount due to or from each member as a result of its activities during the month.

2. PARTNERSHIPS' DELIVERY OBLIGATIONS

In addition to delineating the percentage of the Partnerships' output which each of the Purchasers was entitled, and obligated, to purchase, the Unit Power Agreements also governed the Partnerships' obligations concerning the delivery of power to the Purchasers.

The Unit Power Agreements specified that the delivery point for the electricity was in Rhode Island at the "point of interconnection with the [EHV/PTF] facilities adjacent to" the Plants. The Partnerships' responsibility for delivering the electricity ended at the transmission substation. Further transmission was the responsibility of the Purchasers, including the cost of using the transmission facilities, which are owned by other NEPOOL members,

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and the line losses resulting from the dissipation of electricity during transmission.

VI. BOARD'S ULTIMATE FINDINGS ON DISPUTED ISSUES

*11 On the basis of the foregoing subsidiary findings, the Board found that electricity is not "tangible personal property" for purposes of G.L. c. 63, § 38. Electricity is not an object that is manufactured; it is a flow of power that is generated by the manipulation of magnetic fields. Electricity has no physical shape, form or geographic location. It has no height, weight, volume or other dimension by which tangible property is typically measured.

Although electricity may be perceived by the senses, such as feeling a shock, it has no form or substance which can be touched. It is of a nature similar to heat, light and sound, all of which can be sensed and even measured but, given their lack of form or substance, would not be considered "tangible."

Electricity generated and injected into the grid is indistinguishable from electricity in the transmission and distribution network. Individual electrons are not created in Rhode Island and delivered to Massachusetts; rather, the Partnerships generate power in Rhode Island that, once injected into the grid, merges with power in the grid produced by other generators and is instantaneously available to consumers throughout the network. One cannot trace the energy generated in Rhode Island and determine by any meaningful standard the ultimate destination of that energy. Concepts such as title, possession and delivery, which are relevant for determining the allocation of sales of tangible personal property under § 38, make little sense in the context of the generation and sale of electric power.

Even if such concepts were applicable to electricity, the evidence of record supports a finding that title and possession of the electricity passed from the Partnerships to the Purchasers in Rhode Island. Under the Unit Power Agreements, the Partnerships completed their performance by delivering the electricity at the EHV/PTF substation in Rhode Island. As members of NEPOOL, it was the Purchasers, not the Partnerships, which had the right to use the transmission facilities owned by other NEPOOL members. It was the Purchasers, not the Partnerships, which were responsible for further transmission of the electricity beyond the Rhode Island substation, including the cost of using all necessary transmission facilities. Further, the Purchasers absorbed the line losses resulting from the dissipation of electricity during transmission beyond the Rhode Island substation. Accordingly, even applying tangible property rules to the sale of electricity would result in the sale taking place in Rhode Island, where title and possession of the electricity was delivered to the Purchasers.

The Commissioner's various attempts to allocate a portion of the Partnerships' electricity sales based on the "reverse dock sale rule," the location of the ultimate retail consumer, or the headquarters of the Purchasers, are flawed because they fail to recognize the nature of both electricity itself and the manner of its sale by the Partnerships to the Purchasers. Electricity is not "shipped" by a "common carrier," as required by the reverse dock sale rule. Rather, it is made available on the grid in the amounts the Purchasers were obligated to purchase and withdrawn from the grid by the Purchasers' customers. The sale of electricity is, in effect, determined by accounting adjustments based on a comparison between how much power a purchaser has made available on the grid and the level of consumption by its customers.

*12 The Partnerships could not know the location of the "ultimate consumer" of the electricity they generated because they were not privy to the records of their Purchasers and, even if they were, the consumer location would not be revealed in the Purchasers' records of the many sales to resellers of electricity. Finally, the location of the Purchasers' headquarters is not a relevant consideration, even if electricity were tangible: it is the place where the seller's delivery obligation is completed, not the headquarters of the purchaser, which determines

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where a sale of tangible personal property takes place.

The Commissioner's difficulty in arriving at a reasonable apportionment approach underscores the fact that the sale of electricity does not fit the model of a sale of tangible personal property under § 38(f). Rather, because electricity lacks a physical form and a precise geographic location, making concepts such as title, possession, and delivery somewhat illusory in this context, the standard under § 38(f) that governs all sales other than sales of tangible personal property best fits the sale of electricity. That standard attributes a taxpayer's gross receipts from income-producing activity to the state in which the taxpayer incurs the greatest proportion of the costs of performing that activity.

The evidence of record in these appeals clearly establishes that the Partnerships incurred all of their costs of performance in Rhode Island; the Commissioner's own witness concedes this fact and he does not attempt to argue otherwise. Accordingly, all of their receipts from the sale of electricity are properly attributable to Rhode Island and none to Massachusetts. Because all receipts from electricity sales are attributable to Rhode Island, no receipts are includible in the numerator of appellants' Massachusetts sales factors and, therefore, appellants' sales factors are zero.

On the basis of the foregoing, the Board issued a decision for the appellants and granted an abatement in the amount of $1,346,993.

OPINION

I. APPORTIONMENT OF NET INCOME UNDER § 38

Pursuant to G.L. c. 63, § 38, appellants are subject to a corporate excise on that part of their net income which is derived from business carried on in Massachusetts. Taxable income derived from Massachusetts business is determined by taking appellants' federal net income, applying the deductions enumerated in G.L. c. 63, § 38(a), and multiplying the result by the three-factor apportionment formula under G.L. c. 63, § 38(c). The apportionment formula is based on the ratio of the corporation's property, payroll, and sales in Massachusetts to its total property, payroll, and sales everywhere. The statutory purpose of the three-factor apportionment formula is "to obtain a fair approximation of the corporate income that is 'reasonably related to activities conducted within [Massachusetts].'" **Boston Professional Hockey Association, Inc. v. Commissioner of Revenue**, 443 Mass. 276, 280, n.7 ("**Boston Professional Hockey Association**") (quoting **Gillette Co. v. Commissioner of Revenue**, 425 Mass. 670, 681 (1997), quoting **Exxon Corp. v. Department of Revenue of Wisc.** 447 U.S. 207, 223 (1980)).

*13 The principal issue raised in these appeals is whether any of the Partnerships' sales of electricity should be treated as Massachusetts sales includible in the numerator of appellants' sales factors under G.L. c. 63, § 38(f) ("§ 38(f)").[FN5] Under § 38(f), the sales factor is a "fraction, the numerator of which is the total sales of the corporation in this commonwealth during the taxable year, and the denominator of which is the total sales of the corporation everywhere during the taxable year."

Appellants, whether properly taxable as business corporations or utility corporations, must include in their apportionment factors appellants' pro rata share of the Partnerships' own factors. See 830 C.M.R. 63.38.1(I)(a) and 830 C.M.R. 63.38.1(13)(formerly 830 C.M.R. 63.38.1(11) in 1995 version of the Regulation). Accordingly, resolution of these appeals requires the Board to determine which, if any, of the Partnerships' sales of electricity were "in this commonwealth."

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Section 38(f) provides two different rules for determining whether a sale is "in this commonwealth," depending on the nature of what is sold. In the case of tangible personal property, the general rule is that the sale takes place where the property is delivered to the purchaser. A sale of tangible personal property is "in this commonwealth" under § 38(f) if "the property is delivered or shipped to a purchaser within this commonwealth regardless of the f.o.b. point or other conditions of sale."[FN6]

The determination of whether sales other than sales of tangible personal property are "in this commonwealth" is subject to a different standard. A sale of property other than tangible property is a Massachusetts sale under § 38(f) if: (1) "the income-producing activity is performed in this commonwealth;" or (2) "the income-producing activity is performed both in and outside this commonwealth and a greater proportion of this income-producing activity is performed in this commonwealth than in any other state, based on cost of performance."

Accordingly, resolution of the principal issue of whether any of the Partnerships' sales of electricity should be treated as Massachusetts sales includible in the numerator of appellants' sales factors depends on three sub-issues: 1) whether sales of electricity are sales of "tangible personal property" or sales "other than sales of tangible personal property" for purposes of § 38(f); 2) if electricity is considered tangible personal property for purposes of § 38(f), whether the electricity was delivered in Massachusetts; and 3) if electricity is not tangible personal property for purposes of § 38(f), whether the greater proportion of the Partnerships' income-producing activity is performed in Massachusetts than in any other state. Because the Board found that all of the Partnerships' income-producing activities were performed in Rhode Island, none of the Partnerships' sales would be Massachusetts sales if electricity is not tangible personal property for purposes of § 38(f). Accordingly, the first sub-issue to be determined is whether electricity is tangible personal property for purposes of § 38(f).

II. ELECTRICITY IS NOT TANGIBLE PERSONAL PROPERTY

A. THE COMMON AND ORDINARY MEANING OF "TANGIBLE PERSONAL PROPERTY" DOES NOT ENCOMPASS ELECTRICITY

*14 Section 38(f) does not provide a definition of "tangible personal property." Further, the regulations construing § 38(f) are silent on the issue of whether electricity is tangible personal property for purposes of the sales factor and no Massachusetts case has addressed this issue.

Where a "dominant statutory term is undefined, 'the Legislature should be supposed to have adopted the common meaning of the word, as assisted by a consideration of the historical origins of the enactment.'" **Commissioner of Revenue v. Houghton Mifflin Company**, 423 Mass. 42, 45 (1996) (**"Houghton Mifflin"**).

In cases dealing with the issue of whether a corporation was engaged in "manufacturing," the Supreme Judicial Court has recognized that electricity is not "tangible" property. In **Westinghouse Broadcasting Company, Inc. v. Commissioner of Revenue**, 382 Mass. 354 (1981) (**"Westinghouse"**), the taxpayer, which owned and operated a television and radio station, claimed that it should be classified as a manufacturing corporation in order to qualify for an investment tax credit under G.L. c. 63, § 31A and a property tax exemption under G.L. c. 59, § 5, cl. Sixteenth (3). The court upheld the Board's denial of manufacturing classification, but noted that:

> The Board in the present case did indeed allow a request for a ruling that "Westinghouse may not be denied manufacturing status merely because its end product is intangible." That proposition conformed to our view that the production of electricity may entail manufacture (see **Boston Gas Co. v. Assessors of Boston**, 334 Mass. 549, 565 (1956); **Boston & Me. R.R. v. Billerica**, 262 Mass. 439, 449 (1928)).

Westinghouse, 382 Mass. at 358.

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In this same context of determining whether a corporation was engaged in manufacture, the court again used electricity as an example of an intangible product of manufacturing activity:

> If it be argued that the definition [of manufacturing] contemplates corporeal or tangible input or output, the taxpayer can cite cases that may read to the contrary - those which consider the production of electricity to involve manufacture.

Houghton Mifflin, 423 Mass. at 48-9, quoting **First Data Corporation v. State Tax Commission**, 371 Mass. 444, 446 (1976) ("**First Data Corporation**").

Courts in other jurisdictions have also recognized in a number of contexts that electricity does not constitute tangible personal property within the ordinary meaning of that term. See, e.g., **Omaha Pub. Power Dist. v. Nebraska Department of Rev.**, 248 Neb. 518, 524-25 (1995) ("**Omaha Pub. Power Dist.**") ("[E]lectricity is a physical phenomenon; it is energy, not matter, and has no mass. Electricity can hardly be called 'tangible,' which means 'capable of being touched'"); **Farrand Coal Co. v. Halpin**, 10 Ill.2d 507, 512 (1957)(while recognizing electricity as personal property, Illinois Supreme Court "has at no time held electricity to be 'tangible' personal property"); **People v. Menagas**, 367 Ill. 330, 338 (1937)("While [electricity] is intangible, it is no less personal property and is within the larceny statute"); **Elgin Airport Inn v. Commonwealth Edison Co.**, 88 Ill. App. 3d 477, 480 (noting that strict liability issue arises "[b]ecause electricity is intangible"); **Miller v. City of Los Angeles**, 185 Cal. 440, 443 (1921) ("Electricity is rather an intangible asset and the word 'property' is perhaps not the most apt word by which to describe the supply of electrical energy thus sought to be acquired for the use of the city").

*15 The recognition by Massachusetts and other state courts that electricity is intangible is consistent with common definitions and understanding of the phrase "tangible personal property." For example, Black's Law Dictionary (8th Ed. 2004) ("Black's") defines "tangible personal property" as

> Corporeal personal property of any kind; personal property that can be seen, weighed, measured, felt, or touched or is any other way perceptible to the senses, such as furniture, cooking utensils, and books.

See also **Houghton Mifflin**, 423 Mass. at 48-9 and **First Data Corporation** 371 Mass. at 446 (equating "corporeal" with "tangible"). In turn, Black's defines "corporeal" to be "[a] term descriptive of such things as have an objective, material existence; perceptible by the senses of sight and touch; possessing a real body." It cannot be reasonably argued that electricity has anything resembling a "body" or that electricity itself is perceptible to the senses of sight and touch, as one might see or touch a piece of furniture, a cooking utensil, or a book.

For example, wind, sunlight, sound, heat, and pain are all perceptible to the senses, but cannot be touched. The effects of electricity can be seen, as in a lightning strike, and felt, as in a shock, but electricity itself cannot be seen or touched because, like wind, sunlight, sound, heat, and pain, it has no physical form or body. See Black's (using "light and electricity" as examples of "movable intangible property," defined as "a physical thing that can be moved but that cannot be touched in the usual sense."); **Omaha Pub. Power Dist.**, 248 Neb. at 531 (Caporale, J. concurring)(electricity "has no such physical substance in the sense those two words are commonly understood... it has no readily discernible physical form in the sense that do items such as axes, books, cloth, desks, elevators, fiddles, gavels, and the like").

Accordingly, electricity is not "tangible" as that word is commonly used and understood and therefore is not "tangible personal property" for purposes of § 38(f).

B. THE ONE CASE THAT HAS ADDRESSED THIS ISSUE IN THE CONTEXT OF A STATE APPORTIONMENT FORMULA HELD THAT ELECTRICITY IS NOT TANGIBLE PROPERTY

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The California State Board of Equalization ("SBE"), in construing statutory provisions substantially identical to § 38(f),[FN7] held that sales of electricity constitute the performance of services, not sales of tangible personal property, and that the treatment of such sales for sales factor purposes is properly determined under the cost-of-performance rule. **In Re Appeal of PacifiCorp,** 2002-SBE-005 (Cal. S.B.E. Sept. 12, 2002) ("**PacifiCorp**").

*16 The taxpayer in **PacifiCorp,** like the Partnerships in these appeals, owned and operated a power plant in a neighboring state. As here, the taxpayer sold electricity under contracts providing for delivery at a substation located in the same state as the generating plant. In rejecting an argument that the taxpayer's sales of electricity should be treated as sales of tangible personal property and that its sales should be taxed on a "destination basis," so that sales to customers located in California would be treated as California sales for apportionment purposes, the SBE held:

> Like the court in Otte [**v. Dayton Power & Co.,** 37 Ohio St. 3d 33 (1988)], we conclude that the sales of electricity here are sales of services that essentially consisted of appellant's setting and keeping in motion, through its generation and transmission facilities, electrically charged particles. Also as in **Otte,** we further conclude that the basic reason the generation and transmission process employed by appellant is appropriately characterized as a service is that the process does not result in either (1) the "creation" in its generation facilities of any such arguably tangible particles or (2) the "injection" of those particles into its transmission facilities.

PacifiCorp, supra.

The **PacifiCorp** analysis and holding are persuasive authority on the issue raised in these appeals. Because electricity lacks physical form and a precise geographic location, concepts such as title, possession, and delivery, which are the lynchpins of apportionment for sales of tangible personal property, are ill-suited to the context of electricity sales. Even the Commissioner, in the context of a sale of electricity for sales tax purposes, recognizes that "as a matter of physics, electricity is not transported in a manner similar to other tangible personal property." See Technical Information Release 98-16. It is only through abstractions, approximations, and assumptions that the Commissioner's auditors could fit the sale of electricity into the tangible personal property model under § 38(f). Given the nature of electricity and the accounting function by which it is considered to be bought and sold, the use of the tangible personal property model does not effectuate the statutory purpose of the § 38(c) apportionment formula of approximating that part of corporate income which is related to Massachusetts activities. See **Boston Professional Hockey Association,** 443 Mass. at 280.

Rather, the standard under § 38(f) that applies to all sales other than sales of tangible personal property is best suited to attributing income from sales of electricity to the state in which appellant performed its income-producing activities. That standard attributes a taxpayer's gross receipts from income-producing activity to the state in which the taxpayer incurs the greatest proportion of the costs of performing that activity. In the present case, the Partnerships incurred all of their costs of performance in Rhode Island. Accordingly, all of their receipts from the sale of electricity are properly attributable to Rhode Island and none to Massachusetts.

C. THE LEGISLATIVE HISTORY OF THE SALES TAX EXEMPTION FOR ELECTRICITY AND CASES IN OTHER CONTEXTS DO NOT ESTABLISH THAT ELECTRICITY IS TANGIBLE PERSONAL PROPERTY

*17 The Commissioner cites legislative and judicial treatment of electricity in contexts other than the corporate excise to support his argument that electricity should be considered tangible personal property for purposes of the sales factor. As described below, these authorities are neither persuasive nor determinative.

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1. SALES TAX TREATMENT OF ELECTRICITY

G.L. c. 64H, § 1 provides that "for purposes of this chapter," the phrase "'tangible personal property' shall also include gas, electricity and steam." The Commissioner initially asserted, in his A&R determination letter and abatement denials, that this sales tax definition supported his treatment of electricity as tangible property for purposes of the corporate excise apportionment factor. However, the sales tax definition is of little aid in analyzing the corporate excise apportionment statute at issue here.

First, § 1 explicitly provides that the definition applies "for purposes of this chapter," that is, the sales tax under Chapter 64H. Limited just to the sales tax context, the provision represents nothing more than a legislative determination that retail sales of electricity should be subject to the sales tax.

Further, § 1 also provides that the definition of tangible personal property for sales tax purposes "also" includes electricity. The clear implication of the use of the word "also" is that what follows is not simply a clarification of the general definition, but rather an addition to that definition. The need for such an addition suggests that the Legislature understood that electricity would not fall within the general definition of tangible personal property.

In his post-trial brief, the Commissioner refined his argument by suggesting that an exemption from sales tax for sales of electricity that was enacted as part of the original sales tax statute in 1966 evidenced a Legislative recognition that electricity would otherwise be considered tangible personal property. The Commissioner essentially argued that the Legislature, by initially providing that electricity should not be treated as tangible personal property under the 1966 version of G.L. c. 64H, § 6(i), revealed that it considered electricity to be tangible personal property.

The fundamental flaw in the Commissioner's initial argument is also present here. The Legislature's 1966 sales tax exemption for electricity under § 6(i), like the current definition of tangible personal property under § 1, is applicable for sales tax purposes. Accordingly, the 1966 exemption, like the current sales tax definition, represents a legislative determination of how sales of electricity should be treated under the sales tax, and sheds no light on whether the Legislature considered electricity to be "tangible personal property" for any other purpose.

*18 Moreover, the Legislature's 1990 amendments to Chapter 64H that eliminated the exemption for sales of electricity belie the notion that the Legislature understood that the meaning of tangible personal property included electricity. If, as the Commissioner argued, electricity was so clearly understood to be tangible personal property, the Legislature could simply have repealed or limited § 6(i), leaving electricity to be taxed as other tangible personal property. Initially, the Legislature did just that, in emergency legislation that was enacted on July 18, 1990. See St. 1990, c. 121, § 47.

The July 18, 1990 amendment to § 6(i) was to take effect on September 1, 1990. St. 1990, c. 121, § 110. However, prior to that effective date, on August 1, 1990, and only weeks after the amendment to § 6(i) was enacted, the Legislature made a further change. Despite the already broad definition of tangible personal property, which included personal property of "any nature" including any "commodities whatsoever," the Legislature amended the definition to specifically include electricity. See St. 1990, c. 150, § 359. The specific inclusion of electricity would be superfluous if, as the Commissioner maintained, the Legislature understood the general meaning of tangible personal property to include electricity. See, e.g. **State Tax Commission v. LaTouraine Coffee Co., Inc.**, 361 Mass. 773, 778 (1972) (recognizing that "[n]one of the words of. . . [the] statute is to be regarded as superfluous" in determining legislative intent).

For the foregoing reasons, the Commissioner's reliance on sales tax definitions is not persuasive on the issue of

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whether electricity is tangible property for purposes of the corporate excise.

2. PROPERTY TAX TREATMENT OF ELECTRICITY GENERATION

The Commissioner also argued that the generation of electricity has historically been treated as a "manufacturing" operation for purposes of the local property tax exemption under G.L. c. 59, § 5, cl. Sixteenth (3) and the investment tax credit for manufacturing corporations under G.L. c. 63, § 31A. See, e.g., **Assessors of Holyoke v. State Tax Comm'n,** 355 Mass. 223, 227 (1969); **Boston Gas Co. v. Assessors of Boston,** 334 Mass. 549, 565 (1956); **Boston & Maine R.R. v. Billerica,** 262 Mass. 439, 447-49 (1928). The Commissioner therefore asserts that the fact that electricity is manufactured indicates that it is tangible personal property.

That electricity is considered to be manufactured for purposes of a local property exemption and qualification for investment tax credits does not answer the question of whether it is tangible personal property. The issue addressed in these cases is whether "manufacturing" was taking place. "Manufacturing" has been defined as "the process of transforming raw or finished materials by hand or machinery, and through human skill and knowledge, into something possessing a new nature and name and adapted to a new use." **Commissioner of Corps. & Tax'n v. Assessors of** Boston, 321 Mass. 90, 94 (1947). There is nothing in the definition which supports the notion that only tangible products result from manufacturing.

*19 In fact, as discussed above, Massachusetts courts have recognized that the generation of electricity is an example of a manufacturing process that results in the production of an intangible product. See **Westinghouse,** 382 Mass. at 358 (holding that Board's ruling that manufacturing status cannot be denied because end product is intangible "conformed to [court's] view that the production of electricity may entail manufacturing"); **Houghton Mifflin,** 423 Mass. at 48-9, and **First Data Corporation,** 371 Mass. at 446 (recognizing that cases that consider the production of electricity to involve manufacture counter the argument that the definition of manufacturing "contemplates corporeal or tangible input or output").

Accordingly, Massachusetts manufacturing cases not only fail to advance the Commissioner's position but in fact support the Board's ruling that electricity is commonly understood to be intangible.

3. CASES HOLDING THAT ELECTRICITY IS A "COMMODITY" OR A "PRODUCT" ARE INAPPOSITE

The Commissioner cites a handful of cases in non-tax contexts to support his proposition that the general meaning of "tangible personal property" includes electricity. These cases fail to establish such a proposition and instead serve to underscore the unique nature of electricity as something quite different from tangible property.

G.E. Lothrop Theatres Co. v. Edison Elec. Illuminating Co. of Boston, 290 Mass. 189 (1935) (**"Lothrop Theatres"**), involved a dispute between an electric company and a building owner over the recovery of certain electric charges billed to both the owner and its tenants. The court noted that there "may be" cases where electricity would be considered "a commodity subject to sale and delivery rather than a service furnished by the generating company." **Lothrop Theatres,** 290 Mass. at 193. At a minimum, this observation indicates that the determination of whether electricity is a commodity or a services depends on the context in which the question is asked; it also can be read to suggest that the court's general understanding of electricity is that it is a service.

The court also said that when electricity is sold, it "may be conceded" that there is "something corresponding to delivery in the sale of a tangible chattel." Id. The need for analogy contradicts the Commissioner's claim that electricity is itself tangible personal property. There is nothing in **Lothrop Theatres** that supports the notion that electricity is so commonly understood to be tangible that it must be so characterized generally or for corpor-

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ate excise purposes.

*20 In **Town of Concord, Mass. v. Boston Edison Co.**, 676 F.Supp. 396 (D.Mass. 1988) ("**Town of Concord**"), the court addressed whether electricity was a "commodity" for purposes of the price restrictions under the Robinson-Patman Act, 15 U.S.C.A. § 13(a). A "commodity" is not necessarily tangible personal property; in fact, it is considerably broader in scope. See **Opinion of the Justices**, 408 Mass. 1201, 1206-11 (1990) (concluding that inclusion of the term "commodities" in Article 4 of the Massachusetts Constitution authorizes taxation of services). In fact, the court in **Town of Concord** pointed out that "electricity is not an obviously tangible" item or product and acknowledged that "the average consumer of electricity" might well believe that "she is paying for a service rather than purchasing a product." Id. at 398.

The court's decision is based on considerations specifically relating to price restrictions under the Robinson-Patman Act, particularly whether electricity, like other items subject to those restrictions, "is a thing bought and sold in the marketplace." Id. The fact that the court determined that, except for not being "an obviously tangible item," "electricity is not significantly different from other items deemed commodities subject to the price discrimination prohibitions of antitrust laws" (Id.) does not mean that electricity should be treated as tangible personal property for purposes of the corporate excise apportionment formula.

The Commissioner's citation of a case holding that electricity is a "product" within the meaning of the strict liability rule in Restatement (Second), Torts, § 402A (1965) is also not helpful. The Wisconsin court in **Ransome v. Wisconsin Elec. Power Co.**, 87 Wis.2d 605 (1979), while never using the term "tangible personal property," relied on public policy grounds to support its decision in favor of the consumer-plaintiff. The public policy grounds supporting a ruling of strict liability have no relevance to the issue in the present appeals.

The remaining cases cited by the Commissioner, holding that electricity can be measured, add nothing to the analysis. The fact that electricity can be measured is not contested and does not answer the question of whether it is tangible personal property. If there is anything significant about the subject of measurability, it is that electricity is measured in a manner - the passage or use of current over time - that does not remotely resemble the measurements - height, weight, volume, number of items, etc. - that apply to items of tangible personal property.

II. EVEN IF ELECTRICITY IS PROPERLY CONSIDERED TANGIBLE PERSONAL PROPERTY FOR PURPOSES OF § 38(f), THE PARTNERSHIPS' SALES TOOK PLACE IN RHODE ISLAND, NOT MASSACHUSETTS

*21 The tangible property rule under § 38(f) attributes sales to the state in which the taxpayer completes its delivery to the purchaser. Under the Unit Power Agreements with the Purchasers, the Partnerships effected delivery of the electricity they generated and sold at a specific interconnection point with the NEPOOL grid, the EHV/PTF substation in Rhode Island. At that point, the Purchasers took responsibility for further transmitting the electricity, including the cost of using all NEPOOL transmission facilities and the line losses from dissipation of power during transmission beyond the Rhode Island substation. Accordingly, the Partnerships completed their delivery obligations, and the Purchasers took possession of the electricity, in Rhode Island.

The Commissioner argues that NEPOOL acted as a "common carrier" that "picked up electricity" from the Partnerships in Rhode Island and delivered it to customers in Massachusetts. If a seller hires a "common carrier" to ship goods to a buyer, the sale occurs at the buyer's location, where the property is delivered to the buyer. See 830 C.M.R. 63.38.1(9)(c)1. However, if a buyer "uses its own truck and driver or hires its own carrier to pick up" the property, the sale occurs at the seller's location, when the buyer or the carrier it hires picks up the prop-

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erty. Id.

Apart from the awkwardness of fitting the sale of electricity into a model that uses concepts such as "pick up," "truck," "driver," and "carrier," the common carrier analogy fails on a number of fronts. First, the Purchasers, not the Partnerships, were members of NEPOOL that had both the right to use other NEPOOL members' transmission facilities and the contractual responsibility to transmit the electricity beyond the Rhode Island substation. To the extent that the NEPOOL grid could be considered a "truck" or "carrier," it was a carrier hired by the Purchasers that delivered the electricity.

Further, neither NEPOOL nor the NEPOOL transmission grid fit the definition of a "common carrier" which, according to Black's, is one who is:

> required by law to convey passengers or freight without refusal if the approved fee or charge is paid... One who holds himself out to the public as engaged in business of transportation of persons or property from place to place for compensation.

See also **National Private Truck Council, Inc. v. Commissioner of Revenue**, 426 Mass. 324, 325, n. 1 (1997) ("common carrier" is a "for-hire" transporter of goods). There is nothing in the record to suggest that NEPOOL is required by law to make its facilities available to the general public or any non-member, such as the Partnerships, that is willing to pay the cost of transmission. Only members, such as the Purchasers, that have accepted the terms of the NEPOOL Agreement may use the transmission grid. Accordingly, to the extent that NEPOOL can be viewed as a "carrier" that "shipped" the electricity, it was the Purchasers, as members of NEPOOL that were also contractually responsible for transmitting the electricity beyond the Rhode Island substation, that "hired" the carrier.

*22 Further, the Partnerships cannot be considered as having a responsibility to deliver the electricity to retail customers because, unlike a seller that arranges for the shipment of goods to a purchaser, the Partnerships have no idea of the identity or location of the ultimate purchaser. The ultimate destination of the electricity generated by the Partnerships is the location of the Purchasers' customers, if not the customers of the Purchaser's customers. The identity and location of the Purchasers' wholesale and retail customers is not reasonably ascertainable by the Partnerships. Accordingly, the Partnerships cannot be viewed as having "delivered" the electricity to these entities.

Accordingly, even if, contrary to the Board's finding and ruling, electricity is properly considered "tangible personal property" for purposes of § 38(f), the Partnerships' sales of electricity would still be attributable to Rhode Island, where their delivery obligation to the Purchasers was satisfied.

III. CONCLUSION

On the basis of the foregoing, the Board ruled that electricity is not "tangible personal property" for purposes of the sales factor of the corporate excise apportionment formula under § 38(f). Accordingly, the Partnerships' sales of electricity are attributed to the state in which the Partnerships incur the greatest proportion of their cost of performing their income-producing activity. Because, on the basis of the record, the Partnerships incurred all of their costs of performance in Rhode Island, their receipts from electricity sales are properly treated as Rhode Island, not Massachusetts, sales. Accordingly, no receipts are includible in the numerator of appellants' Massachusetts sales factors and, therefore, appellants' sales factors are zero. The Board, therefore, issued a decision for appellants in these appeals.

By: Frank J. Scharaffa

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Commissioner

Donald E. Gorton, III
Commissioner

Nancy T. Egan
Commissioner

James D. Rose
Commissioner

FN1. The other appellants are National Grid USA Service Company, Inc. (formerly known as New England Power Service Company), TCPL OSP Ltd. (formerly known as Narragansett Energy Resources Company), TCPL OSL, Ltd. and TCPL Power Ltd.

FN2. The periods at issue for each appellant are as follows:
EUA, tax years 1994 through 1998;
TCPL OSP, tax years 1994 and 1996 through 1998;
National Grid, tax years 1994, 1997 and 1998;
TCPL OSL, tax years 1997 and 1998;
TCPL Power, tax years 1994 through 1998.

FN3. A second issue, which is moot if appellants prevail on the sales factor issue, is whether appellants should be taxed as utility corporations under G.L. c. 63, 52A, rather than as business corporations under G.L. c. 63, 32 and 39.

FN4. Each of the Purchasers also purchased electricity from other sources and each of the Purchasers other than TCPM also generated electricity.

FN5. Given the Board's ruling in favor of appellants on this issue, the issue of whether appellants should be taxed in Massachusetts as utility corporations under G.L. c. 63, 52A, rather than as business corporations under G.L. c. 63, 32 and 39, is moot.

FN6. Pursuant to the so-called "throwback rule" under 38(f), a sale of tangible personal property is also a Massachusetts sale if the tangible personal property is delivered or shipped to a purchaser outside the commonwealth, but the corporation is not taxable in the state of delivery and the property was not sold by an agent or agencies operating out of premises owned or rented by the corporation outside of Massachusetts. Neither party argued that the throwback rule was applicable to these appeals.

FN7. Regarding sales of tangible personal property, 25135 of the California Revenue & Tax Code provides that:
Sales of tangible personal property are in this state if:
(a) The property is delivered or shipped to a purchaser, other than the United States government, within this state regardless of the f.o.b. point or other conditions of the sale.
(b) The property is shipped from an office, store, warehouse, factory, or other place of storage in this state and (1) the purchaser is the United States government or (2) the taxpayer is not taxable in the state of the purchaser.
For sales of property other than tangible personal property, 25136 of the California Revenue & Tax Code

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provides that:

Sales, other than sales of tangible personal property are in this state if:

(a) The income-producing activity is performed in this state; or

(b) The income-producing activity is performed both in and outside this state and a greater proportion of the income-producing activity is performed in this state than in any other state, based on costs of performance.

2006 WL 1085380 (Mass.App.Tax.Bd.)

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RECYCLED PAPER
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Expert Report

Prepared by

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Atlanta – January 09, 2012

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I. Introduction

Electrical/electromagnetic devices are widely used today by people in their everyday lives to cover a variety of their needs: from washing/drying their clothes and illuminating houses, to warming up food, talking to friends on a cell phones and watching the news or a favorite movie on a TV set. All of this is possible due to electricity and magnetism or more precisely, the electromagnetic force that exists in our physical universe (the latter is governed by four fundamental forces: nuclear; electromagnetic; weak-interaction; and gravitational).

Electricity has been known since the 6th century B.C. when *Thales of Miletus* (624 B.C.-546 B.C.), an ancient Greek philosopher and mathematician, wrote that when a piece of amber was rubbed in wool it attracted light objects such as straws and feathers (we know now that this is a manifestation of an electrostatic force by friction). Magnetism was also known in ancient Greece, as rocks that attracted pieces of iron or other pieces of similar rock had been observed. It was not until 1600 A.D. that the term "electric" appeared in a treatise on the electric force generated by friction, authored by *William Gilbert* a physician to Queen Elizabeth I (he christened it electricity from the Greek word for amber, "electron", in honor of Thales' experiments). It was not until a century later (1752 A.D.) that one of our founding fathers and greatest scientists of modern times, *Benjamin Franklin*, demonstrated that lightning is a form of electricity and also introduced the terms of positive and negative charges to account for the fact that some materials would repel while others would attract after rubbing a piece of amber with various materials (silk, wool etc.). By that time it was also understood that charges create an electric field. Electrical forces were first investigated systematically by *Charles de Coulomb*, a colonel in the Engineering Corps of the French Army, in 1784, who found experimentally that the intensity of the electric force between two charges is proportional to the product of their charges and inversely proportional to the square of the distance R between them (the unit of charge was named Coulomb in his honor). The electric force is in the direction of the line that connects the two charges.

In the early 1800s, scientists understood how electric currents induce magnetism and *Joseph Henry* (an American physicist and first secretary of the Smithsonian Institution) developed the first electric motor and discovered electromagnetic induction (he also assisted *Morse* in the development of the telegraph). Shortly thereafter, *Michael Faraday* (an English physicist and chemist doing similar experiments as Henry) built the first electric generator (the converse of the electric motor) and published his results in 1831 (before Henry published his). Faraday in essence demonstrated that a changing magnetic field induces an electric field. His device (the Faraday wheel) was the world's first dynamo or electric generator. It was Faraday's discovery, more than any other one, that allowed electricity to be transformed from a topic of scientific curiosity for the few to a powerful technology utilized by everybody.

In 1873, *James Clerk Maxwell*, a Scottish physicist and the greatest name in electromagnetic theory, incorporated into his four famous equations all the experimental findings of the previous scientists that represent the foundation of classical electromagnetic theory (he also proved experimentally that a changing electric field must be accompanied by a changing magnetic field). Maxwell's theory predicted the existence of electromagnetic waves which are the foundation for wireless and wired telecommunications, electric power transmission, laser

systems, medical systems (e.g., MRI) and other applications. He also concluded that light is an electromagnetic wave.

II. Analysis

Since it was clearly understood from the various 19th century experiments that electricity is very practical and convenient, various devices and systems based on electricity were developed to accommodate humankind's needs. The first and most important application was the generation, transmission and distribution of electric energy to households for lighting and heating purposes, as well as providing prime mover energy in the form of electric motors. Another application was energy delivery to industrial customers for manufacturing and control purposes. Power companies, like *Duke Energy Corporation ("Duke Energy")*, are in the business of performing the above functions. These companies are essentially in the business of first transforming kinetic/mechanical energy into electric energy, and then transmitting, distributing and delivering the electric (electromagnetic) energy in an efficient and economical way. The process typically involves three steps: generation, transmission and distribution. Electric energy generation is based on *Faraday's* experiment and basically involves the transformation of kinetic/mechanical energy to electric energy via a time varying magnetic field. The kinetic/mechanical energy is provided by turbines that can turn/rotate from waterfalls (hydroelectric plants), wind (wind generators) or steam pressure (steam is created by burning coal or by causing a controlled nuclear reaction that heats up a water tank). An alternative method is to use solar cells that transform solar energy to electric energy. One should emphasize here that the electric generator is efficiently transforming energy from one form to the other (**a fundamental law of physics is the conservation of energy and the fact that energy cannot be created or destroyed - it simply exists**), and as such the entire generation process deals with energy that already exists in nature.

The electric generator typically consists of a loop of wires that can rotate inside a steady magnetic field (the magnetic field is provided either by permanent magnets or electromagnets/coils - this is called **the stator**). This loop of wires (**the rotor**) is connected to the turbine that makes them rotate once in motion. This motion causes electromagnetic induction (per *Faraday*) between the two ends of the wire loop. Individual slip rings are fitted to each of the two ends of the rotor's wire loop to provide a path for the electric current to leave the armature. Brushes (which are actually carbon contacts) ride against the slip rings and complete the path for the current into the circuit to which the generator is attached. Once this electric energy is generated it must be transmitted and delivered efficiently and safely to the various customers. This is extremely important as losses in the transmission and distribution systems will make the whole system impractical (meaning customers would not get the amount of energy they need) and expensive. For this reason, the transmission system consists of metal wires (lines) that connect the generator to the substations (transformers) and customer (load). The latter are needed to increase the generator voltage prior to transmission and decrease it prior to delivery (transformers operate only with AC voltage/current). *Why?* At home we use a voltage of 110V (60 Hz frequency) or 220V (50 Hz frequency). If the same voltage was used to transmit the electric energy from the generator to our house over a length of several hundreds or thousands of miles the energy would be lost and transformed into heat instead of arriving at our

house since larger amounts of currents would be needed on the lines (large amounts of currents produce more heat) for the same amount of power. For this reason, the generator voltage is increased to 100KV/230KV/525KV, thus, decreasing the required current. The same amount of power is transmitted however (electric power is the product of voltage with current). Before delivery, another transformer reduces the high voltage to the desired one (24 KV, 12 KV or 240V/120V).

It should be emphasized here that the above system is the most efficient one to safely transmit large amounts of electric (electromagnetic) energy over large distances. The same phenomenon applies when we talk on a cell phone but at different power levels and frequencies (1 GHz instead of 60 Hz). A cell phone receives electromagnetic energy (electricity) from the antenna of the base station, and transmits energy back when we talk. The electric energy propagates without the need of any material in between. Experiments have established the fact that electric and magnetic energy can propagate in the form of waves even in vacuum (no material is needed). Actually, this is how we know that other galaxies or star systems exist in outer space. However, for more efficient and safe energy transmission in everyday life the system shown below is used:

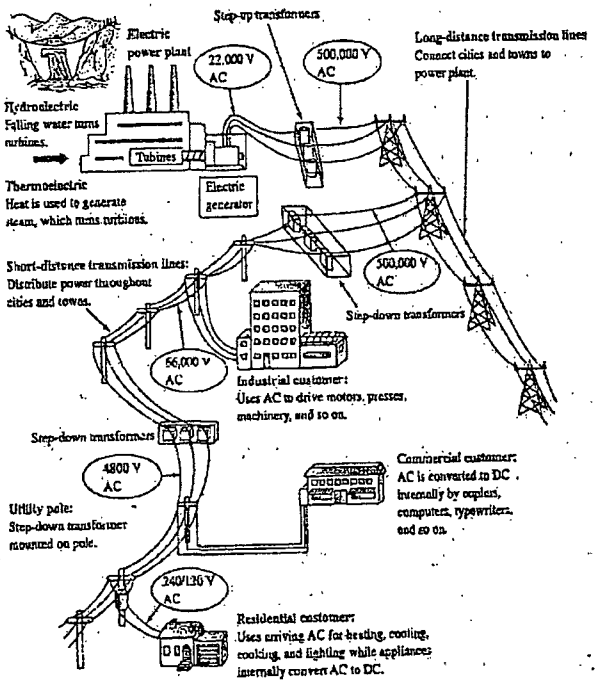
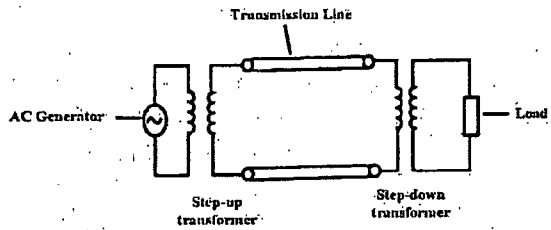


Diagram of basic electric energy supply system [1].



Simple equivalent circuit model.

16288309.1

The electric generator creates an alternating (AC) voltage potential (voltage) that is applied on the transmission line. The line consists of two parallel metal wires. Transformers are inserted between the generator and input of the line to step-up the voltage, and between the end of line and the load to step-it down (simplest form). The AC voltage is required in order to operate the transformers (DC voltage cannot be used). The wires are made out of conducting material (metal such as copper or aluminum). Conductors can transmit/propagate electromagnetic energy very effectively and safely. This is due to the fact that they have electrons loosely associated with the nucleus of their atoms that jump from one atom to the other in the same direction when an electric field is present, thus, creating a net electric current and propagating the electromagnetic energy.

When no electric potential exists, the electrons move in random directions and with varying speeds, thus, producing a zero average current and not propagating any energy. When an AC voltage is applied between the two wires, the electrons flow forward and backward or oscillate at a rate of 60 cycles (times) per second. **The direction of flow in the wires does not matter, as energy is propagated as long as there is a flow of electrons.** *Again, it should be emphasized that other systems/set-ups can be used for this type of energy transmission that are not as efficient as the conducting wires* (One such system/set-up is free space used in propagation of the Sun's visible and non-visible rays that carry electromagnetic energy. Another system/set-up is the usage of free space to propagate electromagnetic waves and energy in wireless communication systems, e.g., cell phones or wireless internet or a radio, between a transmitter and a receiver).

At the load end, this electric field is delivered with the desired strength after step-down voltage conversion. **It should be noted here that electrons are NOT delivered to the load (generally speaking the presence of electrons is not even necessary for electromagnetic energy propagation - electromagnetic energy can propagate in vacuum as in the case of the Sun's rays and wireless communication systems).** Electrons are already part of the transmission line material, as well as the material used in the customer's device (e.g., a motor windings in a washer or a filament in a light bulb). **Electrons facilitate the energy propagation and make it extremely efficient. The entire system delivers energy in the form of an electromagnetic field (or electromagnetic force to be consistent with the four fundamental forces in our physical universe: nuclear, electromagnetic, weak-interaction and gravitational).**

One should also emphasize here that according to a fundamental law of physics and probably the most important one, energy exists in our physical universe and cannot be created or destroyed - it can only be transformed from one form to the other. This electromagnetic field can then be used by our device for the intended purpose. The latter is best illustrated by a household that turns on lights, or operates a TV or operates a washer/drier motor. A substantial and fundamental operation/service that *Duke Energy* performs is the voltage transformation in the various stages of the system to efficiently and safely deliver electric energy to its customers (i.e., minimize the energy losses). Without this transformation, the delivery of large amounts of energy over large areas (e.g., entire countries or even continents) would not be possible. Furthermore, another extremely important operation/service that *Duke Energy* performs is to

successfully meet its customers' energy requirements over time. It is well known that the energy demands (i.e., loads) of the various customers (residential, industrial, etc.) can significantly change over a certain period of time. An extremely important service that *Duke Energy* performs is to accommodate these energy demands by being able to always deliver the required amounts of energy.

As part of my expert report I was also asked to answer the following question: Can the sale of electricity provided by Duke Energy be considered as manufacturing and the sale of tangible personal property, where manufacturing involves the creation of a new and substantially different article having a distinctive name and substantially different character or use?

In the analysis provided in the previous section, it was made clear that companies like *Duke Energy* provide to their customers energy in the form of an electromagnetic field. One of the most fundamental laws of Physics mandates that energy is conserved and it cannot be created or destroyed (it simply exists). As such, *Duke Energy* transforms kinetic/mechanical energy (from burning coal and creating high pressure steam that rotates/moves a turbine) into electromagnetic energy that it then transmits over long distances and distributes to its customers. *Duke Energy* is not delivering electrons or metal wires to its customers. It is also not delivering batteries to its customers. The purpose of the metal wires of the power lines is to efficiently and safely propagate the electromagnetic energy from the power plant to the final delivery point. As a result, transformed energy (kinetic to electromagnetic) is being delivered to the customer and not a substantially different article that has a distinctive name and a substantially different character (to compare one could think of wood abundantly found in nature and creating chairs or tables that are a substantially different article - this is not the case here). In addition, tangible personal property is something that has physical dimensions and one can posses (e.g., a chair, a table, a book, a car).

To better understand, let us make a few comparisons: tangible personal property, in my opinion, is a battery which is an electric charge storage device (one can posses it and it has specific dimensions). A capacitor, another electric energy storage device, is also tangible personal property (one can posses it and it has specific dimensions). *Duke Energy* is not delivering batteries or capacitors to its customers as part of the service it provides. Tangible personal property is a personal computer or a laptop that uses electric energy to operate. Duke Energy is not delivering laptops or computers to its customers under the service it provides. Tangible personal property is water (I can posses it and it has dimensions). To compare, if one opens a hole in the water line/pipe water will leak. Electrons or matter will not leak when a hole is poked in the conductor of a transmission line system used by *Duke Energy*.

To further clarify that the sale of electricity provided by *Duke Energy* cannot be considered as manufacturing or sale of tangible personal property let us consider the following: electric energy can be harvested with an antenna from telecommunication or radio signals that exist around us. However, energy conversion efficiency will be low, thus, the delivered energy will be low and may not be enough to cover the specific needs of the customers. These systems can harvest electromagnetic energy existing in free space or in the vicinity of transmission lines

to power up low energy devices (e.g., a sensor that measures temperature/humidity or a sensor that measures voltage and current in smart grid power systems).

III. Conclusions

Based on the previous analysis it is my opinion that what *Duke Energy* provides is a service, and that the electric energy it sells is not something that one can possess or does not have physical dimensions (e.g., a table, a chair, a book, a car). The service that *Duke Energy* provides is to transform existing energy form one form to the other, and to transmit and distribute that energy in a safe and efficient manner to its customers.

References

[1] *Power Transmission: Mechanical, Hydraulic, Pneumatic, and Electrical*, Thomas E. Scott, Prentice-Hall, 2000.

[2] *Fundamentals of Applied Electromagnetics*, Fawwaz T. Ulaby, Eric Michielssen and Umberto Ravaioli, Prentice-Hall, 2010.

Exhibit U

STATE OF SOUTH CAROLINA
ADMINISTRATIVE LAW COURT

DUKE ENERGY CORPORATION,

Petitioner,

vs. DOCKET NO. 10-ALJ-17-0270-CC

SOUTH CAROLINA DEPARTMENT OF REVENUE,

Respondent.

D E P O S I T I O N

WITNESS: DHIAA M. JAMIL

DATE: January 17, 2012

TIME: 10:37 a.m.

LOCATION: Law Offices of
Nexsen Pruet
227 West Trade Street
Charlotte, North Carolina

TAKEN BY: Attorneys for the Defendants

REPORTED BY: Carolyn M. Beam
Court Reporter

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Can you explain to me the origin of that view?

A. Well, the origin of that view comes from my understanding of what energy is. Energy is the ability to do work. And it cannot be created; it cannot be destroyed. And on that basis, we provide electric energy. We do not create anything, we just change one form of energy into another that is useful to the end user.

You know, a good example that I have, that I -- you know, the image that I have in my mind it's a -- you know, a conversion of energy is a -- a farmer plowing his field chooses to use an ox to pull a plow. That -- I don't think anybody would argue that that ox is providing a service rather than providing a product. Would you agree? I would assume everyone would agree that this is a -- a service.

Q. I'm going to let you answer the questions today.

A. Sure. So what happens with the ox is one form of energy is transformed into a different form of energy. Each -- it eats the -- the food, which is energy, one form of energy, it converts, internally, that form of energy into mechanical

energy that can get work done.

That is as close as to the service that we provide. We take a form of energy that is potentially imbedded in oil, gas, coal or nuclear, wind or sun and we convert it into a form of energy that can perform work. And we charge you on the basis of your enjoyment of that, just like a farmer would charge on the basis of how much was plowed. So that's where the time element comes in. It's a service on the basis of the amount of time that you enjoyed it.

Q. Okay. Was -- was the concept of producing electricity as manufacturing, was that ever a topic or a service? Was that ever a topic of discussion at any of your classes in school?

A. No, I don't think so.

Q. Not that you recall?

A. Not that I recall.

Q. How do you talk about electricity on a day-to-day basis, when you're talking to subcontractors or contractors or employees, how do you refer to electricity?

MR. TRESH: Objection as to form.

THE WITNESS: I refer to it as energy.

BY MR. GREEN:

Exhibit V

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Excerpts From Title 12,
South Carolina Code Annotated (Supp. 2011)

1. **S.C. Code Ann. § 12-4-310**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 4. The South Carolina Department of Revenue
Article 3. General Powers and Duties
§ 12-4-310. Mandated powers and duties.

> The department shall: ...
>
> (10) make available to the authorities of a municipality or county in this State levying a tax based on ***gross*** receipts or net taxable sales, any records indicating the amount of ***gross*** receipts or net taxable sales reported to the department; provided, however, that income tax records may be made available only if the department first has satisfied itself that the ***gross*** receipts reported to the municipality or county were less than the ***gross*** receipts as indicated by the records of the department.

(Emphasis added.)

2. **S.C. Code Ann. § 12-6-40**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 1. Adoption of Internal Revenue Code--Definitions
§ 12-6-40. Application of federal Internal Revenue Code to State tax laws.

> (A)(2)(b) For purposes of Internal Revenue Code Sections 67 (Two Percent Floor on Miscellaneous Itemized Deductions), 71 (Alimony and Separate Maintenance Payments), 85 (Unemployment Compensation), 165 (Losses), 170 (Charitable Contributions), 213 (Medical and Dental Expenses), 219 (Retirement Savings), 469 (Passive Activity Losses and Credits Limited), and 631 (Gain or Loss in the Case of Timber, Coal, or Domestic Iron Ore), "Adjusted ***Gross*** Income" for South Carolina income tax purposes means a taxpayer's adjusted ***gross*** income for federal income tax purposes without regard to the adjustments required by Article 9 and Article 17 of this chapter.

3. **S.C. Code Ann. § 12-6-560**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 5. Tax Rates and Imposition
§ 12-6-560. Computation of resident individual's gross, adjusted gross, and taxable income.

> A resident individual's South Carolina ***gross*** income, adjusted ***gross*** income, and taxable income is computed as determined under the Internal Revenue Code with the modifications provided in Article 9 of this chapter and subject to allocation and apportionment as provided in Article 17 of this chapter.

(Emphasis added.)

4. **S.C. Code Ann. § 12-6-570**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 5. Tax Rates and Imposition
§ 12-6-570. Computation of nonresident individual, trust, estate, and beneficiary's gross, adjusted gross, and taxable income.

> A nonresident individual, nonresident trust, nonresident estate, and nonresident beneficiary's South Carolina ***gross*** income, adjusted ***gross*** income, and taxable income is computed as provided in Section 12-6-1720.

(Emphasis added.)

5. **S.C. Code Ann. § 12-6-580**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 5. Tax Rates and Imposition
§ 12-6-580. Computation of corporation's gross and taxable income.

> A corporation's South Carolina ***gross*** income, taxable income, and the unrelated business income of a corporation exempt from taxation under Internal Revenue Code Section 501 *et seq.*, is computed as determined under the Internal Revenue Code with the modifications provided in Article 9 of this chapter and subject to allocation and apportionment as provided in Article 17 of this chapter.

(Emphasis added.)

6. **S.C. Code Ann. §§ 12-6-590**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 5. Tax Rates and Imposition
§ 12-6-590. Treatment of "S" corporations for tax purposes; shareholders; fund established.

> (A) Except as provided in Section 12-6-1210(F), an "S" Corporation having a valid federal election under the Internal Revenue Code Subchapter "S" is not subject to tax under this chapter to the extent it would be exempt from federal corporate income tax. Each shareholder shall include its share of South Carolina "S" Corporation income on the shareholder's income tax return. All of the provisions of the Internal Revenue Code apply to determine the ***gross*** income, adjusted ***gross*** income, and taxable income of an "S" Corporation and its shareholders subject to the modifications provided in Article 9 of this chapter and subject to allocation and apportionment as provided in Article 17 of this chapter. . . .

(Emphasis added.)

7. **S.C. Code Ann. § 12-6-600**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 5. Tax Rates and Imposition
§ 12-6-600. Taxation of partnerships.

> An entity treated as a partnership for federal income tax purposes is not subject to tax under this chapter. Each partner shall include its share of South Carolina partnership income on the partner's respective income tax return. All of the provisions of the Internal Revenue Code apply to determine the ***gross*** income, adjusted ***gross*** income, and taxable income of a partnership and its partners, subject to the modifications provided in Article 9 of this chapter and subject to allocation and apportionment as provided in Article 17 of this chapter.

(Emphasis added.)

8. **S.C. Code Ann. § 12-6-610**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 5. Tax Rates and Imposition
§ 12-6-610. Computation of gross and taxable income of resident estate or trust.

> A resident estate or resident trust's South Carolina ***gross*** income and taxable income is computed as determined under the provisions of the Internal Revenue Code, including the provisions of Internal Revenue Code Section 584 (Common Trust Funds), with the modifications provided in Article 9 of this chapter and subject to allocation and apportionment as provided in Article 17 of this chapter.

(Emphasis added.)

9. **S.C. Code Ann. § 12-6-620**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 5. Tax Rates and Imposition
§ 12-6-620. Computation of gross, adjusted gross, and taxable income of nonresident individual, trust, and estate.

> A nonresident individual, nonresident trust, and nonresident estate's South Carolina ***gross*** income, adjusted ***gross*** income, and taxable income is computed as provided in Section 12-6-1720.

(Emphasis added.)

10. **S.C. Code Ann. § 12-6-1110**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation (Refs & Annos)
Chapter 6. South Carolina Income Tax Act
Article 9. Taxable Income Calculation
§ 12-6-1110. Modifications of gross, adjusted gross, and taxable income calculated under Internal Revenue Code; federal Section 1354 elections.

> (A) For South Carolina income tax purposes, ***gross*** income, adjusted ***gross*** income, and taxable income as calculated under the Internal Revenue Code are modified as provided in this article and subject to allocation and apportionment as provided in Article 17 of this chapter. . . .

(Emphasis added.)

11. **S.C. Code Ann. § 12-6-1120**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 9. Taxable Income Calculation
§ 12-6-1120. Gross income; computation; modifications.

> South Carolina ***gross*** income is computed by making modifications to ***gross*** income provided in the Internal Revenue Code as follows:
>
> (1) The exclusion from ***gross*** income authorized by Internal Revenue Code Section 103 (Interest on State and Local Bonds) is modified to exempt only interest on obligations of this State or any of its political subdivisions, and to exempt interest upon obligations of the United States. This modification applies to all Internal Revenue Code Sections referencing Section 103
>
> (2) South Carolina ***gross*** income does not include any state income tax refund included in federal ***gross*** income. . . .
>
> (4) South Carolina ***gross*** income is determined without application of Internal Revenue Code Sections 78 (***Gross***-up of Dividends received from Certain Foreign Corporations), 86

(Social Security and Tier 1 Railroad Retirement Benefits), and 87 (Alcohol Fuel Credit). . . .

(7) South Carolina ***gross*** income does not include compensation or retirement benefits received from the United States or any state for service in a state National Guard or a reserve component of the Armed Forces of the United States. . . .

(8) Each partner in the Palmetto Seed Capital Fund Limited Partnership (Fund) established pursuant to Section 41-44-60 shall exclude from South Carolina ***gross*** income seventy-five percent of the partner's proportionate share of income the fund derives from a South Carolina business which is either: (i) established and operated in a least developed county as defined in Section 12-6-3360; or (ii) invested in agriculture, aquaculture, or a related business or in a business created by a socially or economically disadvantaged individual as defined in 13 Code of Federal Regulations, Sections 124.105(A) and 124.106 (1987). . . .

(10) South Carolina ***gross*** income does not include the amounts excluded by Section 59-4-100 of the South Carolina Tuition Prepayment Program.

(Emphasis added.)

12. **S.C. Code Ann. § 12-6-1130**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 9. Taxable Income Calculation
§ 12-6-1130. Taxable income; computation; modifications.

South Carolina taxable income is computed by making modifications to deductions provided in the Internal Revenue Code as follows: . . .

(8) Adjusted ***gross*** income and taxable income are computed without the deductions for certain unused business credits authorized by Internal Revenue Code Section. . . .

(13) Adjusted ***gross*** income and taxable income are computed without the deduction allowed pursuant to Internal Revenue Code Section 199 relating to domestic production activities. . . .

(Emphasis added.)

13. **S.C. Code Ann. § 12-6-1140**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 9. Taxable Income Calculation
§ 12-6-1140. Deductions from individual taxable income.

> There is allowed as a deduction in computing South Carolina taxable income of an individual the following: . . .
> (4) amounts included in South Carolina ***gross*** income received for disability retirement due to permanent and total disability by a person who could qualify for the homestead exemption under Section 12-37-250 by reason of being classified as totally and permanently disabled; . . .

(Emphasis added.)

14. **S.C. Code Ann. § 12-6-1210**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 9. Taxable Income Calculation
§ 12-6-1210. Deductions for capital expenses, depreciation, gains and losses; change in accounting method; certain elections for special tax treatment; provisions of federal law.
. . .

> (M) For a taxable year beginning after December 31, 1984, to the extent ***gross*** income, adjusted ***gross*** income, or taxable income of any taxpayer is affected by a provision of federal law enacted before January 1, 1985, which provision is not contained in the Internal Revenue Code, the provision is applicable in determining the South Carolina ***gross***, adjusted ***gross***, and taxable income of the taxpayer in the appropriate taxable year. . . .

(Emphasis added.)

15. **S.C. Code Ann. § 12-6-1720**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation

Chapter 6. South Carolina Income Tax Act
Article 13. Nonresident and Part-Year Resident Individuals
§ 12-6-1720. Taxable income of nonresident individual, trust, estate, or beneficiary; modifications, adjustments, and allocations.

> A nonresident individual, a nonresident trust, a nonresident estate, and a nonresident beneficiary shall report and compute South Carolina taxable income as a resident taxpayer of this State subject to the following modifications: . . .
>
> (2) The South Carolina taxable income of a nonresident individual, nonresident estate, or nonresident trust must be adjusted as follows:
>
> (a)(i) For a nonresident individual, the personal exemptions and the applicable standard deduction or itemized deductions must be reduced to an amount which is the same proportion as South Carolina adjusted ***gross*** income is to federal adjusted ***gross*** income.
>
> (ii) For a nonresident estate or nonresident trust, the personal exemption and itemized deductions must be reduced to an amount which is the same proportion as South Carolina ***gross*** income is to federal ***gross*** income.
>
> (b) For purposes of the computation in item (2)(a), South Carolina adjusted ***gross*** income means the adjusted ***gross*** income of the taxpayer calculated as provided in Section 12-6-1720(1). Adjustments to ***gross*** income authorized by Internal Revenue Code Section 62 must be apportioned based on the ratio of South Carolina ***gross*** income to federal ***gross*** income. However, if the adjustment is directly connected with an item of ***gross*** income, the adjustment is allowed only to the extent the item of income is taxable in this State. . .

(Emphasis added.)

16. **S.C. Code Ann. § 12-6-2260**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 17. Allocation and Apportionment
§ 12-6-2260. Definition of property factor; tangible personal property; determination of value of property.

. . .

(D) For purposes of this section, value of property is determined as follows: . . .

(3) For rented and leased real and personal property, value is the net annual rental rate multiplied by eight. For rented or leased personal property the department may require a factor other than a multiplier of eight to be used if it better reflects the value.

Net annual rental rate means the ***gross*** annual rate paid by the taxpayer, less the ***gross*** annual rental rate received by the taxpayer for any subrentals of real estate. . . .

(Emphasis added.)

17. **S.C. Code Ann. § 12-6-2290**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 17. Allocation and Apportionment
§ 12-6-2290. Apportionment of remaining net income where principal profits or income derived from sources not otherwise described by this chapter.

<For tax years through 2010, this section reads as follows:>

If the principal profits or income of a taxpayer are derived from sources other than those described in Section 12-6-2250 or Section 12-6-2310, the taxpayer shall apportion its remaining net income using a fraction in which the numerator is ***gross*** receipts from within this State during the taxable year and the denominator is total ***gross*** receipts from everywhere during the taxable year. For purposes of this section, items included in ***gross*** receipts are as provided in Section 12-6-2295.

<Effective for tax years after 2010, this section reads as follows:>

If the principal profits or income of a taxpayer are derived from sources other than those described in Section 12-6-2252 or Section 12-6-2310, the taxpayer shall apportion its remaining net income using a fraction in which the numerator is ***gross*** receipts from within this State during the taxable

year and the denominator is total ***gross*** receipts from everywhere during the taxable year. For purposes of this section, items included in ***gross*** receipts are as provided in Section 12-6-2295.

(Emphasis added.)

18. **S.C. Code Ann. § 12-6-2295**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 17. Allocation and Apportionment
§ 12-6-2295. Items included and excluded from terms "sales" and "gross receipts".

(A) The terms "sales" as used in Section 12-6-2280 and "***gross*** receipts" as used in Section 12-6-2290 include, but are not limited to, the following items if they have not been separately allocated:

(1) receipts from the sale or rental of property maintained for sale or rental to customers in the ordinary course of the taxpayer's trade or business including inventory;

(2) receipts from the sale of accounts receivable acquired in the ordinary course of trade or business for services rendered or from the sale or rental of property maintained for sale or rental to customers in the ordinary course of the taxpayer's trade or business if the accounts receivable were created by the taxpayer or a related party. For purposes of this item, a related person includes a person that bears a relationship to the taxpayer as described in Section 267 of the Internal Revenue Code;

(3) receipts from the use of intangible property in this State including, but not limited to, royalties from patents, copyrights, trademarks, and trade names;

(4) net gain from the sale of property used in the trade or business. For purposes of this subsection, property used in the trade or business means property subject to the allowance for depreciation, real property used in the trade or business, and intangible property used in the trade or business which is:

(a) not property of a kind that properly would be includible

in inventory of the business if on hand at the close of the taxable year; or

(b) held by the business primarily for sale to customers in the ordinary course of the trade or business;

(5) receipts from services if the entire income-producing activity is within this State. If the income-producing activity is performed partly within and partly without this State, sales are attributable to this State to the extent the income-producing activity is performed within this State;

(6) receipts from the sale of intangible property which are unable to be attributed to any particular state or states are excluded from the numerator and denominator of the factor.

(B) The terms "sales" as used in Section 12-6-2280 and "***gross*** receipts" as used in Section 12-6-2290 do not include:

(1) repayment, maturity, or redemption of the principal of a loan, bond, or mutual fund or certificate of deposit or similar marketable instrument;

(2) the principal amount received under a repurchase agreement or other transaction properly characterized as a loan;

(3) proceeds from the issuance of the taxpayer's stock or from sale of treasury stock;

(4) damages and other amounts received as the result of litigation;

(5) property acquired by an agent on behalf of another;

(6) tax refunds and other tax benefit recoveries;

(7) pension reversions;

(8) contributions to capital, except for sales of securities by securities dealers;

(9) income from forgiveness of indebtedness; or

(10) amounts realized from exchanges of inventory that are not recognized by the Internal Revenue Code,

(Emphasis added.)

19. **S.C. Code Ann. § 12-6-2310**
Code of Laws of South Carolina 1976 Annotated

Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 17. Allocation and Apportionment
§ 12-6-2310. Income remaining after allocation for certain companies; factors to be used for apportionment.

. . .

> (3) Telephone service companies shall use a fraction in which the numerator is ***gross*** receipts in this State during the taxable year and the denominator is total ***gross*** receipts everywhere. The term "***gross*** receipts in this State" includes ***gross*** revenues derived from services rendered wholly within this State, plus that portion of the company's interstate revenues attributable to this State in accordance with the Federal Communications Standard Classification of Accounts. . . .

(Emphasis added.)

20. **S.C. Code Ann. § 12-6-2810**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 21. Foreign Trade Receipts
§ 12-6-2810. Deferral of taxes on income attributable to increase in gross income from foreign trading receipts.

> Payment of tax otherwise due under this chapter on income attributable to the increase in ***gross*** income from foreign trading receipts may be deferred until the taxpayer intentionally ceases exporting property, or until after three taxable years in which the taxpayer has no ***gross*** income from foreign trading receipts, whichever is earlier, provided the base amount defined in Section 12-6-2850(3) does not exceed five million dollars, and the taxpayer pays interest annually on the aggregate deferred tax at the base period T-bill rate. The interest is due on the date the taxpayer is required to file the annual return required by this chapter without regard to any extension.

(Emphasis added.)

21. **S.C. Code Ann. § 12-6-2850**

Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation (Refs & Annos)
Chapter 6. South Carolina Income Tax Act
Article 21. Foreign Trade Receipts
§ 12-6-2850. Definitions.

> For purposes of this article:
>
> (3) "Increase in ***gross*** income from foreign trading receipts" is the amount by which the ***gross*** income from foreign trading receipts during the applicable tax year exceeds a base amount equal to the average of annual ***gross*** income from foreign trading receipts over the three taxable years before the applicable taxable year. . .

(Emphasis added.)

22. **S.C. Code Ann. § 12-6-3360**

Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 25. Credits
§ 12-6-3360. Job tax credit.
. . .

> (C)(2)(a) Subject to the conditions provided in subsection (M) of this section, a job tax credit is allowed for five years beginning in year two after the creation of the job for each new full-time job created if the minimum level of new jobs is maintained. The credit is available to taxpayers with ninety-nine or fewer employees that increase employment by two or more full-time jobs, and may be received only if the ***gross*** wages of the full-time jobs created pursuant to this section amount to a minimum of one hundred twenty percent of the county's or state's average per capita income, whichever is lower. No credit is allowed for the year or any subsequent year in which the net employment increase falls below the minimum level of two. The amount of the initial job credit is as described in subsection (C)(1).
>
> (b) If the taxpayer with ninety-nine or fewer employees increases employment by two or more full-time jobs but the ***gross*** wages do not amount to a minimum one hundred twenty percent of the county's or state's average per capita

income, whichever is lower, then the amount of the initial job credit is as follows:
(i) Four thousand dollars for each new full-time job created in "Tier IV" counties.
(ii) Two thousand one hundred twenty-five dollars for each new full-time job created in "Tier III" counties.
(iii) One thousand three hundred sev enty-five dollars for each new full-time job created in "Tier II" counties.
(iv) Seven hundred fifty dollars for each new full-time job created in "Tier I" counties. . . .

(Emphasis added.)

23. **S.C. Code Ann. § 12-6-3380**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 25. Credits
§ 12-6-3380. Tax credit for child and dependent care expenses.

An individual may claim an income tax credit for child and dependent care expenses. The credit is computed as provided in Internal Revenue Code Section 21, except that the term "applicable percentage" means seven percent and is not reduced, and only expenses that are directly attributable to items of South Carolina ***gross*** income qualify for the credit.
. . .

(Emphasis added.)

24. **S.C. Code Ann. § 12-6-3575**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 25. Credits
§ 12-6-3575. Health insurance tax credits.
. . .

(D) A taxpayer who claims the credit allowed by this section shall provide information required by the department to demonstrate that the taxpayer is eligible for the credit and that the amount paid for premiums for which the credit is claimed was not excluded from the taxpayer's ***gross*** income

for the taxable year. . . .

(Emphasis added.)

25. **S.C. Code Ann. § 12-6-3670**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 25. Credits
§ 12-6-3670. Credit for excess premium paid for property and casualty insurance.
. . .

> (B) For the purposes of computing the credit allowed by this section, excess premium paid is the amount by which the premium paid exceeds five percent of the taxpayer's adjusted ***gross*** income.

(Emphasis added.)

26. **S.C. Code Ann. § 12-6-4910**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 6. South Carolina Income Tax Act
Article 37. Tax Returns
§ 12-6-4910. Persons, corporations, and other entities required to make tax returns.

> Income tax returns must be filed by the following:
>
> (1)(a) an individual not listed in subitem (c) who has a ***gross*** income for the taxable year of at least the federal ex-emption amount plus the applicable basic standard deduction, plus any deduction the taxpayer qualifies for pursu-ant to Section 12-6-1170(B), without regard to a reduction for the retirement income deduction, and whose filing status is:
> (i) single, surviving spouse, or head of household; or
> (ii) married, filing separately, and whose spouse does not itemize deductions.
>
> (b) an individual not listed in (c) who files a joint return and whose combined ***gross*** income for the taxable year, is more than the sum of twice the exemption amount plus the applicable basic standard deduction if the individ-ual and spouse had the same household at the close of the taxable year, plus any deduction the taxpayer quali-fies for pursuant to Section

12-6-1170(B). If the individual or spouse is sixty-five or older, the standard deduc-tion is increased as provided in Internal Revenue Code Section 63(c)(3) and 63(f)(1).

(c) an individual listed below whose ***gross*** income exceeds the federal personal exemption amount:
(i) an individual making a return under Internal Revenue Code Section 443(a)(1) for less than twelve months because of a change in the individual's annual accounting period;
(ii) an individual described in Internal Revenue Code Section 63(c)(5) (Certain Dependents) who has un-earned income in excess of the amount provided in Internal Revenue Code Section 63(c)(5)(A), or who has total ***gross*** income in excess of the standard deduction;
(iii) an individual for whom the standard deduction is zero.

(d) a nonresident individual with South Carolina ***gross*** income greater than the personal exemption amount pro-vided in Internal Revenue Code Section 151(d). . . .

(3) an "S" Corporation conducting business in South Carolina, having South Carolina ***gross*** income, or subject to the license fee requirements of Chapter 20 of this title, or having an interest in any partnership conducting business in this State.

(4) a partnership conducting business in this State, having South Carolina ***gross*** income or having an interest in any partnership conducting business in this State.

(5) an estate with a nonresident beneficiary or with ***gross*** income for the taxable year of six hundred dollars or more.

(6) a trust with a nonresident beneficiary, any taxable income, or with ***gross*** income of six hundred dollars or more regardless of the amount of taxable income.

(7) an estate of an individual under Chapters 7 or 11 of Title 11 of the United States Code relating to bankruptcy with ***gross*** income for the taxable year of two thousand seven hundred dollars or more.

(Emphasis added.)

27. **S.C. Code Ann. § 12-6-4940**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation

Chapter 6. South Carolina Income Tax Act
Article 37. Tax Returns
§ 12-6-4940. Trust institutions maintaining common trust fund must make tax return; contents.

> Every trust institution maintaining a common trust fund shall make a return under oath for each taxable year. The return shall contain the items of ***gross*** income and the deductions allowed by law, the names and addresses of the participants, and the proportionate share of taxable income for each participant.

(Emphasis added.)

28. **S.C. Code Ann. § 12-8-510**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 8. Income Tax Withholding
Article 5. Withholding Required
§ 12-8-510. Parties subject to withholding laws.

> A person located, doing business, or having ***gross*** income in this State and an employer having an employee earning income within this State are subject to the withholding laws provided in this chapter.

(Emphasis added.)

29. **S.C. Code Ann. § 12-8-520**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 8. Income Tax Withholding
Article 5. Withholding Required
§ 12-8-520. Incomes subject to withholding and amounts to be withheld.
. . .

> (D) For purposes of this chapter "wages" is all remuneration for services of any nature performed by an employee for an employer, including the fair market value of all remuneration paid in a medium other than cash, except the term does not include remuneration paid: . . .
>
> (3) for personal services performed in this State by nonresident employees in connection with their regular employment

outside of this State when the ***gross*** South Carolina wages are equal to or less than the personal exemption amount provided in Internal Revenue Code Section 151(d) as defined in Section 12-6-40.

(10) for payments to a self-employed retirement fund (Keogh Plans) or to an individual retirement account or program as permitted under the Internal Revenue Code if, at the time of the payment, it is reasonable to believe that the amounts are excludable or deductible from South Carolina ***gross*** income; . . .

(Emphasis added.)

30. **S.C. Code Ann. § 12-8-600**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 8. Income Tax Withholding
Article 5. Withholding Required
§ 12-8-600. Withholding from any type of payment included in state gross income not specified in chapter; agreement by payee and payor; properly executed withholding exemption certificate deemed request for withholding.

(A) A payee and payor may enter into an agreement to withhold income tax from any type of payment not otherwise provided in this chapter that is includable in South Carolina ***gross*** income. The agreement is effective for a mutually agreed upon period unless the payor or payee furnishes a signed written notice to the other party terminating the agreement. . . .

(Emphasis added.)

31. **S.C. Code Ann. § 12-10-30**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 10. Enterprise Zone Act of 1995
§ 12-10-30. Definitions.

As used in this chapter: . . .

(4) " ***Gross*** wages " means wages subject to withholding. . .

(Emphasis added.)

32. **S.C. Code Ann. § 12-10-45**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 10. Enterprise Zone Act of 1995
§ 12-10-45. Designation of census tract by tire manufacturer as enterprise zone; certification of tire manufacturer.

> A tire manufacturer that has over one billion dollars in capital investment in this State, and employs over five thousand workers in this State may, after certification by the council, designate up to two census tracts, but not to exceed four hundred acres per site, in any area of the State as an enterprise zone provided that a capital investment of at least one hundred million dollars be made over a five-year period at each site. The tire manufacturer's capital investment must be based upon the ***gross*** cost of assets in South Carolina as shown on the manufacturer's property tax and fee-in-lieu of property tax filings. The council will certify the manufacturer if it determines that the available incentives are appropriate for the new project, the total benefits of the new project exceed the costs to the public, and the qualifying business otherwise fulfills the requirements of this chapter.

(Emphasis added.)

33. **S.C. Code Ann. § 12-10-80**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 10. Enterprise Zone Act of 1995
§ 12-10-80. Job development credits.
. . .

> (B)(1) The maximum job development credit a qualifying business may claim for new employees is limited to the lesser of withholding tax paid to the State on a quarterly basis or the sum of the following amounts:
>
> (a) two percent of the ***gross*** wages of each new employee who earns $8.74 or more an hour but less than $11.64 an hour;
>
> (b) three percent of the ***gross*** wages of each new employee

who earns $11.65 or more an hour but less than $14.55 an hour;

(c) four percent of the ***gross*** wages of each new employee who earns $14.56 or more an hour but less than $21.84 an hour; and

(d) five percent of the ***gross*** wages of each new employee who earns $21.85 or more an hour. . . .

(C) To claim a job development credit, the qualifying business must incur qualified expenditures at the project or for utility or transportation improvements that serve the project. To be qualified, the expenditures must be: . . .

(3) used for any of the following purposes: . . .

(f) employee relocation expenses, but only for those employees to whom the company is paying ***gross*** wages at least two times the lower of the per capita income for either the state or the county in which the project is located; . . .

(Emphasis added.)

34. **S.C. Code Ann. § 12-10-81**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 10. Enterprise Zone Act of 1995
§ 12-10-81. Job development tax credits.

. . .

(C)(1) The maximum job development credit a qualifying business may claim for new employees is determined by the sum of the following amounts:

(a) two percent of the ***gross*** wages of each new employee who earns $6.95 or more an hour but less than $9.27 an hour;

(b) three percent of the ***gross*** wages of each new employee who earns $9.27 or more an hour but less than $11.58 an hour;

(c) four percent of the ***gross*** wages of each new employee who earns $11.58 or more an hour but less than $17.38 an hour;

(d) five percent of the ***gross*** wages of each new employee

who earns $17.38 or more an hour; and

(e) the increase in the state sales and use tax of the business from the year of the effective date of its revitalization agreement pursuant to this section and subsequent years, over its state sales and use tax for the first of the three years preceding the effective date of this revitalization agreement. . . .

(Emphasis added.)

35. **S.C. Code Ann. § 12-10-85**

Code of Laws of South Carolina 1976 Annotated Title 12. Taxation Chapter 10. Enterprise Zone Act of 1995 § 12-10-85. Purpose and use of State Rural Infrastructure Fund; grants.

(A) Funds received by the department for the State Rural Infrastructure Fund must be deposited in the State Rural Infrastructure Fund of the council. The fund must be administered by the council for the purpose of providing financial assistance to local governments for infrastructure and other economic development activities including, but not limited to: . . .

(7) relocation expenses, but only for those employees to whom the company is paying ***gross*** wages at least two times the lower of the per capita income for either the state or the county in which the project is located. . . .

(Emphasis added.)

36. **S.C. Code Ann. § 12-16-20**

Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 16. Estate Tax
Article 1. Definitions and Domicile
§ 12-16-20. Definitions.

As used in this chapter, unless the context clearly shows otherwise, the term or phrase:

(3) "***Gross*** estate" means "***gross*** estate" as defined in Internal Revenue Code § 2031. . . .

(9) "Personal representative" means the personal representative of the estate of the decedent, appointed, qualified, and acting within the State, or, if there is no personal representative appointed, qualified, and acting within the State, then any person in actual or constructive possession of the South Carolina ***gross*** estate of the decedent. . . .

(Emphasis added.)

37. **S.C. Code Ann. § 12-16-510**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 16. Estate Tax
Article 5. Imposition of Tax
§ 12-16-510. Estates of residents.
. . .

(B) If any real and tangible personal property of a resident is located outside of this State and is subject to a death tax imposed by another state for which the federal credit is allowed, the amount of the tax due under this section must be credited with the lesser of:

(1) the amount of the death tax paid the other state and credited against the federal estate tax; or

(2) an amount computed by multiplying the federal credit by a fraction, the numerator of which is the value of that part of the ***gross*** estate over which another state or states have jurisdiction to the same extent to which this State would exert jurisdiction under this chapter with respect to the residents of the other state or states and the denominator of which is the value of the decedent's ***gross*** estate. . . .

(Emphasis added.)

38. **S.C. Code Ann. § 12-16-520**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 16. Estate Tax
Article 5. Imposition of Tax
§ 12-16-520. Estates of nonresidents.

(A) A tax in an amount computed as provided in this section

is imposed on the transfer of every nonresident's tax-able estate located in this State.

The tax is an amount computed by multiplying the federal credit by a fraction, the numerator of which is the value of that part of the ***gross*** estate over which this State has jurisdiction for estate tax purposes and the denominator of which is the value of the decedent's ***gross*** estate. . . .

(Emphasis added.)

39. **S.C. Code Ann. § 12-16-530**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 16. Estate Tax
Article 5. Imposition of Tax
§ 12-16-530. Estates of aliens.

(A) A tax in an amount computed as provided in this section is imposed upon the transfer of real property and tangible personal property having an actual situs in this State and upon intangible personal property physically present within this State of every person who at the time of death was not a resident of the United States.

The tax is an amount computed by multiplying the federal credit by a fraction, the numerator of which is the value of that part of the ***gross*** estate over which this State has jurisdiction for estate tax purposes and the denominator of which is the decedent's ***gross*** estate taxable by the United States wherever situated. . . .

(Emphasis added.)

40. **S.C. Code Ann. § 12-16-720**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 16. Estate Tax
Article 7. Tax on Generation-Skipping Transfers
§ 12-16-720. Imposition of tax.

. . .

(B) A tax is imposed upon every generation-skipping transfer where the original transferor is not a resident of this State

at the date of the original transfer, but where the generation-skipping transfer includes real or personal property having a situs in this State, in an amount equal to the maximum amount allowable as a credit for state generation-skipping transfer taxes under Internal Revenue Code § 2604, reduced by an amount which bears the same ratio to the total state tax credit allowable for federal generation-skipping transfer tax purposes as the value of the transferred property taxable by all other states bears to the value of the ***gross*** generation-skipping transfer for federal generation-skipping transfer tax purposes. In any case in which a tax is imposed on a generation-skipping transfer by this State and by one or more other states, the department shall negotiate with the taxing authorities of the other state or states so that the aggregate amount of taxes imposed by this State and the other state or states on a generation-skipping transfer does not exceed one hundred percent of the maximum amount allowable as credit for state generation-skipping transfer taxes under Internal Revenue Code § 2604.

(Emphasis added.)

41. **S.C. Code Ann. § 12-16-910**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 16. Estate Tax
Article 9. Recapture Tax on Certain Use-Valuations
§ 12-16-910. Tax treatment of certain farm or business realty; filing requirements; additional tax upon disposition or discontinuance of qualified uses of property.

(A) When the ***gross*** estate of a decedent at the date of death is a value requiring filing a federal estate tax return and the estate contains certain farm or business real property which qualified for valuation under Internal Revenue Code Section 2032A for the tax imposed under this chapter, a copy of the election made at the time of filing the federal estate tax return, if made, must be attached to the South Carolina estate tax return when filed. The return shall also include an agreement signed by each person in being having an interest, whether or not in possession, in the property and consent to the application of Internal Revenue Code Section 2032A. . .

(Emphasis added.)

42. **S.C. Code Ann. § 12-16-1220**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 16. Estate Tax
Article 11. Returns and Payment of Tax
§ 12-16-1220. Information to be furnished by probate judge.

> The probate judge shall send to the department by mail a copy of the inventory and appraisal of the assets of every estate the ***gross*** assets of which for probated purposes are equal to or exceed the sum of six hundred thousand dollars within thirty days after it is filed, together with a copy of any will probated with respect to the estate. In the case of a nonresident decedent, the probate judge shall furnish the department with copies of all wills filed with his office and, in the case of an ancillary administration, the probate judge shall furnish the department with copies of inventories and appraisals in all cases regardless of the value of the tangible personal property and real property having a situs in this State.

(Emphasis added.)

43. **S.C. Code Ann. § 12-20-100**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 20. Corporation License Fees
§ 12-20-100. License tax on utilities and electric cooperatives; tax based on value of property; additional tax based on gross receipts; payment; consolidated or combined return; minimum license fee.

> (A) In the place of the license fee imposed by Section 12-20-50, every express company, street railway company, navigation company, waterworks company, power company, electric cooperative, light company, gas company, telegraph company, and telephone company shall file an annual report with the department and pay a license fee as follows: . . .
>
> (2)(a) three dollars for each thousand dollars, or fraction of a thousand dollars, of ***gross*** receipts derived from ser-vices rendered from regulated business within this State during the

preceding taxable year, except that with regard to electric cooperatives, only distribution electric cooperatives are subject to the ***gross*** receipts portion of the license fee under this subitem (2)(a).

(b) When a consolidated return is filed pursuant to Section 12-6-5020, the phrase "the ***gross*** receipts derived from services rendered from regulated business" does not include ***gross*** receipts arising from transactions be-tween the separate members of the return group; . . .

(Emphasis added.)

44. **S.C. Code Ann. § 12-20-110**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 20. Corporation License Fees
§ 12-20-110. Chapter provisions inapplicable to certain organizations, companies and associations.

The provisions of this chapter do not apply to any: . . .

(6) foreign corporation whose entire income is excluded from ***gross*** income for federal income tax purposes due to a treaty obligation of the United States; . . .

(Emphasis added.)

45. **S.C. Code Ann. § 12-21-2420**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 21. Stamp and Business License Tax
Article 17. Admissions Tax
§ 12-21-2420. Imposition of tax; rate; exemptions; payment, collection, and remittance; disposition of revenues.

There must be levied, assessed, collected, and paid upon paid admissions to places of amusement within this State a license tax of five percent. The license tax may be listed separately from the cost of admission on an admission ticket. However, no tax may be charged or collected: . . .

(11) On admissions to events other than those events enumerated in item (4) of this section, sponsored and operated

exclusively by eleemosynary, nonprofit corporations or organizations organized exclusively for religious, charitable, scientific, civic, fraternal, or educational purposes when the net proceeds derived from admissions to the events shall be immediately donated to an organization operated exclusively for charitable purposes. The term "net proceeds" shall mean the portion of the ***gross*** admissions proceeds remaining after necessary expenses of the event have been paid. This item shall not apply to an event in which the above organizations receive a percentage of ***gross*** proceeds or a stated fixed sum for the use of its name in promoting the event. . . .

(Emphasis added.)

46. **S.C. Code Ann. § 12-21-2830**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 21. Stamp and Business License Tax
Article 21. Collection and Enforcement Generally
§ 12-21-2830. Record required of gross receipts; record subject to inspection; violations.

Every person subject to a tax imposed by this chapter shall keep a record showing the value and the ***gross*** receipts derived from engaging in any business taxable under this chapter as shall be required by the department and such record shall at all times be subject to inspection by any agent of the department. . . .

(Emphasis added.)

47. **S.C. Code Ann. § 12-21-3920**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 21. Stamp and Business License Tax
Article 24. Regulation of Bingo Games
§ 12-21-3920. Definitions.

As used in this article: . . .

(21) "Site system" means a computer accounting system commonly referred to as a point of sale system used in conjunction with electronic dabbers. This computer software must be used at a site by an organization which al-lows a

bingo ticket purchased from a licensed distributor to authorize the download or activation of faces into the electronic dabbers, accounts for ***gross*** proceeds, and provides accounting information on all activity for one year from the end of the quarter in which the activity occurred. . . .

(Emphasis added.)

48. **S.C. Code Ann. § 12-21-4000**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 21. Stamp and Business License Tax
Article 24. Regulation of Bingo Games
§ 12-21-4000. Procedures applicable to conduct of bingo.

In addition to the manner of play prescribed in Section 12-21-3990, the following procedures apply to the conduct of the game: . . .

(12)(a) At least fifty percent of the ***gross*** proceeds of the sale of bingo cards taken in by the house during a single session must be returned to the players in the form of prizes. However, with respect to fair licenses, this requirement must be met during the course of the fair.

(b) A bingo operation may take in only two times more in ***gross*** proceeds than the prize for that session aver-aged on a quarterly basis. Amounts in excess of this limit are subject to a tax, in addition to any other bingo license taxes and fees equal to the amount of the excess. Each session that the ***gross*** proceeds are greater than twice the prize amounts paid constitutes a separate offense if the tax is unpaid. . . .

(Emphasis added.)

49. **S.C. Code Ann. § 12-21-4007**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 21. Stamp and Business License Tax
Article 24. Regulation of Bingo Games
§ 12-21-4007. Site system and electronic dabber specifications.

(A) A site system and an electronic dabber must meet the

following specifications:

(1) A site system must:

(a) record a nonresetable electronic consecutive six digit receipt number for each transaction;

(b) issue a player a receipt for each transaction containing the: (i) name of a site or organization; (ii) date and time of transaction; (iii) number of electronic bingo card images downloaded or activated; (iv) selling price of a card or package, ***gross*** proceeds, and receipt number; and (v) serial number of device issued to a player;

(c) print a summary report for each session containing: (i) the date and time of the report; (ii) the name of site; (iii) the date of the session; (iv) the sequential session number; (v) the number of transactions; (vi) the number of voided transactions; (vii) the number of electronic bingo card images downloaded or activated; (viii) the number of devices used; (ix) the total ***gross*** proceeds; and (x) any other information required by the department. . . .

(Emphasis added.)

50. **S.C. Code Ann. § 12-21-4020**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 21. Stamp and Business License Tax
Article 24. Regulation of Bingo Games
§ 12-21-4020. Classes of bingo licenses; taxes.

The following are the classes of bingo licenses: . . .

(5) CLASS E: An organization which has a game of bingo and operates exclusively by bona fide members who are residents of this State and who do so on a strictly volunteer basis and whose ***gross*** bingo proceeds do not exceed forty thousand dollars a calendar quarter, and where prizes do not exceed four thousand dollars a session shall obtain a Class E license from the department at a cost of five hundred dollars. If the ***gross*** bingo proceeds for any calendar quarter exceed thirty thousand dollars, the person or organization within ten days is required to obtain a Class B li-cense from the department and comply with all requirements of a Class B li-

cense. The holder of a Class E license may not conduct more than one bingo session a week.

(6) CLASS F: An organization which has a game of bingo and operates exclusively by bona fide members who are residents of this State and who do so on a strictly volunteer basis and whose ***gross*** proceeds do not exceed forty thousand dollars a calendar quarter, and where prizes do not exceed four thousand dollars a session and where bingo proceeds are only used to pay the organization's utility bills, to pay charges for bingo paper, and for the charitable purpose of the organization, shall obtain a Class F license from the department at the cost of one hundred dollars. The holder of a Class F license may not conduct more than one bingo session a week.

(Emphasis added.)

51. **S.C. Code Ann. § 12-21-4030**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 21. Stamp and Business License Tax
Article 24. Regulation of Bingo Games
§ 12-21-4030. Entrance fee surcharges.

. . .

(C) The entrance fees collected pursuant to subsection (B) are not required to be remitted as taxes and are not included in ***gross*** proceeds for purposes of the prize limitations provided in Section 12-21-4000(12)(a).

(Emphasis added.)

52. **S.C. Code Ann. § 12-21-4080**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 21. Stamp and Business License Tax
Article 24. Regulation of Bingo Games
§ 12-21-4080. Promoter to turn over proceeds; member to deposit proceeds.

(A) Upon completion of the session, the promoter or the organization member representative shall deposit the ***gross*** proceeds from the session less the amount paid out as prizes into the bingo checking account. If the promoter is author-

ized by the organization to make the session deposit, the promoter shall deliver to the organization representative evidence that the deposit was made in a timely manner. This evidence must be furnished no later than the next business day following the day of the bingo session on which the proceeds were obtained. . . .

(Emphasis added.)

53. **S.C. Code Ann. § 12-21-4090**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 21. Stamp and Business License Tax
Article 24. Regulation of Bingo Games
§ 12-21-4090. Bingo checking and savings accounts.
. . .

(I) ***Gross*** proceeds derived from the conduct of bingo must not be commingled with other funds of the licensed organization. . . .

(Emphasis added.)

54. **S.C. Code Ann. § 12-21-4100**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 21. Stamp and Business License Tax
Article 24. Regulation of Bingo Games
§ 12-21-4100. Record keeping and reporting requirements.

(A) Each licensed nonprofit organization conducting bingo games shall submit quarterly to the department on the last day of the month following the close of the calendar quarter a report under oath containing the following information:

(1) the amount of the ***gross*** proceeds derived from the games; . . .

(Emphasis added.)

55. **S.C. Code Ann. § 12-28-110**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation

Chapter 28. Motor Fuels Subject to User Fees
Article 1. Definitions
§ 12-28-110. Definitions.

> As used in this chapter: . . .
>
> (30) "***Gross*** gallons" means the total, measured product, exclusive of temperature or pressure adjustments, considerations or deductions, in United States gallons. . . .

(Emphasis added.)

56. **S.C. Code Ann. § 12-28-1300**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 28. Motor Fuels Subject to User Fees
Article 13. Reports
§ 12-28-1300. Verified statement by supplier; reporting of information.
. . .

> (C) The supplier report required by this section must include the following information, with respect to billed gal-lons of motor fuel subject to the user fee, for all products in the aggregate, and the supplier shall identify if the billed gallon is net or ***gross***: . . .

(Emphasis added.)

57. **S.C. Code Ann. § 12-28-1330**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 28. Motor Fuels Subject to User Fees
Article 13. Reports
§ 12-28-1330. Terminal operator must file monthly sworn statement of operations; annual report.
. . .

> (B) The monthly terminal report required by this section must include the following information for each terminal location in this State: . . .
>
> (3) detail schedules of removals by shipment including: (a) carrier name or alpha code; (b) carrier FEIN; (c) mode of transportation; (d) destination state; (e) supplier responsible for reporter removal; (f) supplier FEIN; (g) date removed

from terminal; (h) document number; (i) net gallons; (j) ***gross*** gallons. . . .

(Emphasis added.)

58. **S.C. Code Ann. § 12-28-1920**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 28. Motor Fuels Subject to User Fees
Article 19. Enforcement Powers
§ 12-28-1920. Operation of permanent or portable weigh stations.

> The department may assign qualified persons who are not state police officers to supervise or operate permanent or portable weigh stations. A person assigned under this section may stop, inspect, and issue citations to operators of trucks and trailers, barges or vessels having a declared ***gross*** weight of eleven thousand pounds or more, and buses, at a permanent weigh station, or other inspection point, or while operating a clearly marked state police vehicle for violations of this chapter.

(Emphasis added.)

59. **S.C. Code Ann. § 12-28-2910**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 28. Motor Fuels Subject to User Fees
Article 29. Economic Development
§ 12-28-2910. South Carolina Coordinating Council for Economic Development; establishing project priorities; disposition of payments.

. . .

> (E) From the amount set aside pursuant to subsection (A), the council is authorized to expend funds which were not obligated or committed as of July first of the current fiscal year only as necessary for the location or expansion of an industry or business facility in South Carolina. Eligible expenditures include water and sewer projects, road or rail construction and improvement projects, land acquisition, fiber-optic cable, relocation of new employees, pollution-control equipment, environmental testing and related due diligence reports, acquiring and improving real property,

and site preparation. Site preparation is defined as surveying, environmental and geotechnical study and mitigation, clearing, filling, and grading. Relocation expenses constitute eligible expenditures only for those employees to whom the company is paying ***gross*** wages at least two times the lower of the per capita income for either the State or the county in which the project is located. . . .

(Emphasis added.)

60. **S.C. Code Ann. § 12-33-245**

Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 33. Alcoholic Beverages Taxes
Article 3. License Taxes for Sale of Alcoholic Beverages
§ 12-33-245. Excise tax on sales for on-premises consumption; "gross proceeds" defined; nonprofit organizations exception; penalties; issuance of license for premises for which license revoked or suspended.

(A) In addition to taxes imposed pursuant to the provisions of Sections 12-33-230, 12-33-240, Article 5 of this chapter, and Chapter 36, Title 12, there is imposed an excise tax equal to five percent of the ***gross*** proceeds of the sales of alcoholic liquor by the drink for on-premises consumption in an establishment licensed for sales pursuant to Article 5, Chapter 6, Title 61 or at a location holding a temporary license or permit that authorizes the sale of liquor by the drink. All proceeds of this excise tax must be deposited to the credit of the general fund of the State. Except with respect to the distribution of the revenue of this tax, this excise tax is considered to be imposed pursuant to Chapter 36, Title 12. For purposes of this subsection, "***gross*** proceeds of sales" has the meaning as provided in Section 12-36-90, except that the sales tax imposed under Chapter 36, Title 12 is not included in "***gross*** proceeds of sales". The term "***gross*** proceeds of sales" also includes, but is not limited to, the retail value of a complimentary or discounted beverage containing alcoholic liquor, an amount charged for ice for a drink containing alcoholic liquor, and an amount charged for a nonalcoholic beverage that is sold or used as a mixer for a drink containing alcoholic liquor. . . .

(D) In addition to all other penalties that may be imposed for

violations arising pursuant to subsection (A) of this section, a failure to report and remit the full amount of the excise tax imposed pursuant to subsection (A) on the ***gross*** proceeds of the sale of each drink of alcoholic liquor sold for consumption in the establishment subjects the licensee to the following penalties: . . .

(Emphasis added.)

61. **S.C. Code Ann. § 12-36-90**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 1. Citation and Definitions
§ 12-36-90. "Gross proceeds of sales".

Gross proceeds of sales, or any similar term, means the value proceeding or accruing from the sale, lease, or rental of tangible personal property. . . .

(Emphasis added.)

62. **S.C. Code Ann. § 12-36-510**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 5. Retail License
§ 12-36-510. Retail license requirements; license tax; "special events".
. . .

(B) A retail license is not required of: . . .

(2) organizations conducting concession sales at festivals if the ***gross*** proceeds of the sales are exempt from sales tax pursuant to Section 12-36-2120(39); . . .

(Emphasis added.)

63. **S.C. Code Ann. § 12-36-910**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 9. Sales Tax

§ 12-36-910. Five percent tax on tangible personal property; laundry services, electricity, communication services, and manufacturer-consumed goods.

(A) A sales tax, equal to five percent of the ***gross*** proceeds of sales, is imposed upon every person engaged or continuing within this State in the business of selling tangible personal property at retail.

(B) The sales tax imposed by this article also applies to the:

(1) ***gross*** proceeds accruing or proceeding from the business of providing or furnishing any laundering, dry cleaning, dyeing, or pressing service, but does not apply to the ***gross*** proceeds derived from coin-operated laundromats and dry cleaning machines;

(2) ***gross*** proceeds accruing or proceeding from the sale of electricity;

(3)(a) ***gross*** proceeds accruing or proceeding from the charges for the ways or means for the transmission of the voice or messages, including the charges for use of equipment furnished by the seller or supplier of the ways or means for the transmission of the voice or messages. ***Gross*** proceeds from the sale of prepaid wireless calling arrangements subject to tax at retail pursuant to item (5) of this subsection are not subject to tax pursuant to this item. Effective for bills rendered after August 1, 2002, charges for mobile telecommunications services subject to the tax under this item must be sourced in accordance with the Mobile Telecommunications Sourcing Act as provided in Title 4 of the United States Code. The term "charges for mobile telecommunications services" is de-fined for purposes of this section the same as it is defined in the Mobile Telecommunications Sourcing Act. All other definitions and provisions of the Mobile Telecommunications Sourcing Act as provided in Title 4 of the United States Code are adopted. Telecommunications services are sourced in accordance with Section 12-36-1920; . . .

(5) ***gross*** proceeds accruing or proceeding from the sale or recharge at retail for prepaid wireless calling arrangements.

(6) ***gross*** proceeds accruing or proceeding from the sale or renewal of warranty, maintenance, or similar service contracts for tangible property, whether or not such contracts

are purchased in conjunction with the sale of tangible personal property.

(7) ***gross*** proceeds accruing or proceeding from the sale or renewal of warranty, maintenance, or similar service contracts for tangible personal property, whether or not the contracts are purchased in conjunction with the sale of tangible personal property.

(C) Notwithstanding other provisions in this article or Article 13, Chapter 36, of this title, the sales or use tax imposed by those articles does not apply to the ***gross*** proceeds accruing or proceeding from charges for or use of data processing. . . .

(Emphasis added.)

64. **S.C. Code Ann. § 12-36-920**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 9. Sales Tax
§ 12-36-920. Tax on accommodations for transients; reporting.

(A) A sales tax equal to seven percent is imposed on the ***gross*** proceeds derived from the rental or charges for any rooms, campground spaces, lodgings, or sleeping accommodations furnished to transients by any hotel, inn, tourist court, tourist camp, motel, campground, residence, or any place in which rooms, lodgings, or sleeping accommodations are furnished to transients for a consideration. This tax does not apply where the facilities consist of less than six sleeping rooms, contained on the same premises, which is used as the individual's place of abode. The ***gross*** pro-ceeds derived from the lease or rental of sleeping accommodations supplied to the same person for a period of ninety continuous days are not considered proceeds from transients. . . .

(D) When any business is subject to the sales tax on accommodations and the business has more than one place of business in the State, the licensee shall report separately in his sales tax return the total ***gross*** proceeds derived from business done within and without the corporate limits of municipalities. A taxpayer who owns or manages rental

units in more than one county or municipality shall report separately in his sales tax return the total ***gross*** proceeds from business done in each county or municipality. . . .

(Emphasis added.)

65. **S.C. Code Ann. § 12-36-950**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 9. Sales Tax
§ 12-36-950. Presumption as to gross proceeds; burden of proof; resale certificate.

It is presumed that all ***gross*** proceeds are subject to the tax until the contrary is established. The burden of proof that the sale of tangible personal property is not a sale at retail is on the seller. . . .

(Emphasis added.)

66. **S.C. Code Ann. § 12-36-1310**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 13. Use Tax
§ 12-36-1310. Imposition of tax; rate; applicability; credit for tax paid in another state.
. . .

(B) The use tax imposed by this article also applies to the:

(1) ***gross*** proceeds accruing or proceeding from the business of providing or furnishing a laundering, dry cleaning, dyeing, or pressing service, but does not apply to the ***gross*** proceeds derived from coin operated laundromats and dry cleaning machines;

(2) ***gross*** proceeds accruing or proceeding from the sale of electricity;

(3)(a) ***gross*** proceeds accruing or proceeding from the charges for the ways or means for the transmission of the voice or messages, including the charges for use of equipment furnished by the seller or supplier of the ways or means for the transmission of the voice or messages. ***Gross***

proceeds from the sale of prepaid wireless calling arrangements subject to tax at retail pursuant to item (5) of this subsection are not subject to tax pursuant to this item. . . .

(5) ***gross*** proceeds accruing or proceeding from the sale or recharge at retail for prepaid wireless calling arrangements. . .

(6) ***gross*** proceeds accruing or proceeding from the sale or renewal of warranty, maintenance, or similar service contracts for tangible personal property, whether or not such contracts are purchased in conjunction with the sale of tangible personal property. . . .

(Emphasis added.)

67. **S.C. Code Ann. § 12-36-1710**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 17. Casual Excise Tax
§ 12-36-1710. Excise tax on casual sales of motor vehicles, motorcycles, boats, motors, and airplanes; exclusions; payment of tax as prerequisite to titling, licensing, or registration.

. . .

(B) Excluded from the tax are: . . .

(3) ***gross*** proceeds of transfers of motor vehicles, motorcycles, or airplanes specifically exempted by Section 12-36-2120 from the sales or use tax; . . .

(Emphasis added.)

68. **S.C. Code Ann. § 12-36-2120**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 21. Maximum Tax and Exemptions
§ 12-36-2120. Exemptions from sales tax.

Exempted from the taxes imposed by this chapter are the ***gross*** proceeds of sales, or sales price of: . . .

(17) machines used in manufacturing, processing, recycling,

compounding, mining, or quarrying tangible personal property for sale. "Machines" include the parts of machines, attachments, and replacements used, or manufactured for use, on or in the operation of the machines and which (a) are necessary to the operation of the machines and are customarily so used, or (b) are necessary to comply with the order of an agency of the United States or of this State for the prevention or abatement of pollu-tion of air, water, or noise that is caused or threatened by any machine used as provided in this section. This exemption does not include automobiles or trucks. As used in this item "recycling" means a process by which materials that otherwise would become solid waste are collected, separated, or processed and reused, or returned to use in the form of raw materials or products, including composting, for sale. In applying this exemption to machines used in recycling, the following percentage of the ***gross*** proceeds of sale, or sales price of, machines used in recycling are exempt from the taxes imposed by this chapter: . . .

(34) fifty percent of the ***gross*** proceeds of the sale of a modular home regulated pursuant to Chapter 43 of Title 23, both on-frame and off-frame. For purposes of this item only, "***gross*** proceeds of sale" equals the manufacturer's net invoice price of the modular home sold, including all accessories built in to the modular home at the time of delivery to the purchaser and not including freight or deposit on returnable materials. The manufacturer shall collect the tax and remit it to the Department of Revenue; . . .

(62) seventy percent of the ***gross*** proceeds of the rental or lease of portable toilets. . . .

(Emphasis added.)

69. **S.C. Code Ann. § 12-36-2130**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 21. Maximum Tax and Exemptions
§ 12-36-2130. Exemptions from use tax.

Exempted from the use tax imposed by Article 13 of this

chapter are the sales prices of:

(1) property the ***gross*** proceeds of sales of which are required to be included in the measure of the tax imposed by the provisions of Article 9 of this chapter and on which the tax has been paid by its seller or retailer. . . .

(Emphasis added.)

70. **S.C. Code Ann. § 12-36-2540**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 25. General Provisions
§ 12-36-2540. Duty to keep records and books.

. . .

(B) Any person selling both at wholesale and at retail shall keep books which separately show the ***gross*** proceeds of wholesale sales and the ***gross*** proceeds of retail sales. If the records are not separately kept, all sales must be considered retail sales. . . .

(Emphasis added.)

71. **S.C. Code Ann. § 12-36-2570**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 25. General Provisions
§ 12-36-2570. Time when tax payment due; monthly report.
. . .

(B) Any person selling both at wholesale and at retail shall keep books which separately show the ***gross*** proceeds of wholesale sales and the ***gross*** proceeds of retail sales. If the records are not separately kept, all sales must be considered retail sales. . . .

(Emphasis added.)

72. **S.C. Code Ann. § 12-36-2645**
Code of Laws of South Carolina 1976 Annotated

Title 12. Taxation
Chapter 36. The South Carolina Sales and Use Tax Act
Article 25. General Provisions
§ 12-36-2645. Taxes applicable to proceeds of 900/976 telephone service; tax rate; disposition of revenues.

> The sales and use taxes imposed by this chapter also extend to ***gross*** proceeds accruing or proceeding from the business of providing 900/976 telephone service except that the applicable rate of the tax is ten percent. All revenues derived from the tax imposed by this section must be credited to the general fund of the State.

(Emphasis added.)

73. **S.C. Code Ann. § 12-37-930**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 37. Assessment of Property Taxes
Article 5. Liability for Taxes; Returns
§ 12-37-930. Valuation of property; depreciation allowances for manufacturer's machinery and equipment; department may permit adjustment in allowance.
. . .

> In no event may the original cost be reduced by more than as provided in Section 12-37-935, except this limit is ninety per-cent for (1) custom molds and dies used in the conduct of manufacturing electronic interconnection component assembly devices for computers and computer peripherals; and (2) equipment used in the manufacture of tires by manufacturers who employ more than five thousand employees in this State and have over one billion dollars in capital investment in this State. Capital investment will be based upon the ***gross*** cost of assets in South Carolina as shown on the manufacturer's property tax and fee-in-lieu of property tax filings. The term "original cost" means ***gross*** capitalized cost, including property on which the taxpayer made the election allowed pursuant to Section 179 of the Internal Revenue Code of 1986, as shown by the taxpayer's records for income tax purposes. . . .

(Emphasis added.)

74. **S.C. Code Ann. § 12-37-2645**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 37. Assessment of Property Taxes
Article 21. Motor Vehicles
§ 12-37-2645. Assessment ratio for determining assessed value of motor vehicle.

> For purposes of determining the appropriate assessment ratio used in the calculation of the assessed value of a motor vehicle and for defining those motor vehicles subject to the assessment ratios provided in Section 1(8)(B)(a) of Article X of the Constitution of this State, the definition of "private passenger motor vehicle" provided in Section 56-3-630 applies except that in the case of pickup trucks, the empty weight and ***gross*** weight limits provided in that definition are increased respectively to nine thousand pounds or less and eleven thousand pounds or less and the definition is deemed to include motorcycles.

(Emphasis added.)

75. **S.C. Code Ann. § 12-37-2810**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 37. Assessment of Property Taxes
Article 23. Motor Carriers
§ 12-37-2810. Definitions.

> As used in this article, unless the context requires otherwise:
> . . .
> (B) "Motor vehicle" means a motor propelled vehicle used for the transportation of property on a public highway with a ***gross*** vehicle weight of greater than twenty-six thousand pounds.

(Emphasis added.)

76. **S.C. Code Ann. § 12-37-2820**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 37. Assessment of Property Taxes
Article 23. Motor Carriers

§ 12-37-2820. Assessment of motor vehicles.

> (A) The Department of Revenue annually shall assess, equalize, and apportion the valuation of all motor vehicles of motor carriers. The valuation must be based on fair market value for the motor vehicles and an assessment ratio of nine and one-half percent as provided by Section 12-43-220(g). Fair market value is determined by depreciating the ***gross*** capitalized cost of each motor vehicle by an annual percentage depreciation allowance down to ten percent of the cost as follows: . . .
>
> (B) "***Gross*** capitalized cost", as used in this section, means the original cost upon acquisition for income tax purposes, not to include taxes, interest, or cab customizing.

(Emphasis added.)

77. **S.C. Code Ann. § 12-43-220**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 43. County Equalization and Reassessment
Article 3. Programs; Uniform Assessment Ratios
§ 12-43-220. Classifications shall be equal and uniform; particular classifications and assessment ratios; procedures for claiming certain classifications; roll-back taxes.

. . .

> (f) Except as specifically provided by law, all other personal property must be taxed on an assessment of ten and one-half percent of fair market value of the property, except that commercial fishing boats, and commercial tugboats and pilot boats must be taxed on an assessment of five percent of fair market value. As used in this item "commercial fishing boats" means boats used exclusively for commercial fishing, shrimping, or crabbing and (1) licensed by the Department of Natural Resources, or (2) on or from which is used commercial fishing equipment licensed by the Department of Natural Resources. As used in this item, "commercial tugboats" shall mean boats used exclusively for harbor and ocean towing, documented with the U.S. Coast Guard, constructed of steel, and being at least seventy-nine feet in length and having a ***gross*** tonnage of at least ninety-nine tons. . . .

(Emphasis added.)

78. **S.C. Code Ann. § 12-43-224**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 43. County Equalization and Reassessment
Article 3. Programs; Uniform Assessment Ratios
§ 12-43-224. Assessment of undeveloped acreage subdivided into lots.

> Notwithstanding the requirement that real property is required by law to be appraised at fair market value for ad valorem tax purposes, when undeveloped acreage is surveyed into subdivision lots and the conditional or final plat is recorded with the appropriate county official, the county assessor shall appraise each lot as an individual property and then discount his ***gross*** actual market value estimate of the developer's lot holdings under the following conditions: . . .

(Emphasis added.)

79. **S.C. Code Ann. § 12-43-227**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 43. County Equalization and Reassessment
Article 3. Programs; Uniform Assessment Ratios
§ 12-43-227. Valuation of homeowners' association property.

> The fair market value of homeowners' association property, as defined in Section 12-43-230, for ad valorem tax purposes is defined as the nonqualified earnings value to be determined by the capitalization of the property's non-qualified ***gross*** receipts. For purposes of this section, "nonqualified ***gross*** receipts", means the ***gross*** receipts from the use of the property other than: . . .
>
> (2) amounts received from the developer of the property owned by the homeowners' association as reported on the most recently filed application submitted pursuant to Section 12-43-230. If additional reporting is required pursuant to Section 12-43-230, nonqualified ***gross*** receipts shall be determined utilizing ***gross*** receipts from the most recent completed tax year. After a piece of property's nonqualified ***gross*** receipts have been established, they must be capital-

ized to determine nonqualified earnings value by utilizing a capitalization rate of twenty percent. Not-withstanding any other provision of this section, in the event of real property with zero or de minimus nonqualified ***gross*** receipts, the special valuation of homeowners' association property shall not result in any homeowners' association property being valued at a rate less than five hundred dollars an acre.

(Emphasis added.)

80. **S.C. Code Ann. § 12-43-230**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 43. County Equalization and Reassessment
Article 3. Programs; Uniform Assessment Ratios
§ 12-43-230. Treatment of agricultural real property, mobile home and lessee improvements to real property; department shall prescribe regulations.

. . .

(d) . . .Homeowners' association property does not come within the provisions of this subsection unless the owners of the real property or their agents make a written application for it on or before the first penalty date for taxes due for the first tax year in which the special valuation is claimed. The application may be with respect to one or any number of tracts or parcels owned by the homeowners' association. The application for the special valuation must be made to the assessor of the county in which the special valuation property is located, on forms provided by the county and approved by the department which includes the reporting of nonqualified ***gross*** receipts, and failure to apply constitutes a waiver of the special valuation for that year. No additional annual filing is required while the property re-mains homeowners' association property and the ownership remains the same, unless the nonqualified ***gross*** receipts within the meaning of Section 12-43-227 for the most recent completed tax year either (i) exceed the amount of nonqualified ***gross*** receipts with respect to the property reported on the most recently filed application by ten percent or more or (ii) are less than ninety percent of the amount of nonqualified ***gross*** receipts with respect to the property reported on the most recently filed application. In that case, the owners of the real property or their agents must make additional written application with

respect to the property and report the change in nonqualified ***gross*** receipts.

(Emphasis added.)

81. **S.C. Code Ann. § 12-43-232**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 43. County Equalization and Reassessment
Article 3. Programs; Uniform Assessment Ratios
§ 12-43-232. Requirements for agricultural use.

> In addition to all other requirements for real property to be classified as agricultural real property, the property must meet the following requirements:
>
> (1)(b) A tract which meets the acreage requirement of subitem (a) of this item devoted to growing Christmas trees is considered timberland. A Christmas tree tract not meeting the acreage requirement qualifies as agricultural property if the landowner reports ***gross*** income from Christmas trees that meets the income test provided in item (3) of this section, mutatis mutandis. . . .
>
> (3)(a) Nontimberland tracts not meeting the acreage requirement of item (2) qualify as agricultural real property if the person making the application required pursuant to Section 12-43-220(d)(3) earned at least one thousand dollars of ***gross*** farm income for at least three of the five taxable years preceding the year of the application. . . .
>
> (b) An owner making an initial application required pursuant to Section 12-43-220(d)(3) for a nontimberland tract of less than ten acres may claim the property as agricultural real property for each year for the first five years of operation if he earned at least one thousand dollars of ***gross*** farm income in at least three of the first five years. . . .

(Emphasis added.)

82. **S.C. Code Ann. § 12-54-155**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 54. Uniform Method of Collection and Enforcement of Taxes Levied and As-

sessed by South Carolina Department of Revenue
§ 12-54-155. Substantial underpayment of tax or substantial valuation misstatement.
. . .

> (C) For purposes of this section, there is a substantial valuation misstatement if the: . . .
>
> (2)(a) price for property or services for use of property claimed on the return in connection with a transaction between persons described in Internal Revenue Code Section 482 is two hundred percent or more, or fifty percent or less, of the amount determined pursuant to Section 482 to be the correct amount of the price; or
>
> (b) net Internal Revenue Code Section 482 transfer price adjustment for the taxable year exceeds the lesser of five million dollars or ten percent of the taxpayer's South Carolina ***gross*** receipts.

(Emphasis added.)

84. **S.C. Code Ann. § 12-60-90**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 60. The South Carolina Revenue Procedures Act
Article 1. General Provisions
§ 12-60-90. Administrative tax process.
. . .

> (D) The department may suspend or disbar from practice in the administrative tax process or censure any person authorized by these rules to represent taxpayers, if the person is shown to be incompetent, disreputable, or fails or refuses to comply with the rules in subsection (E), or in any manner, with intent to defraud, wilfully and knowingly deceives, misleads, or threatens any person or prospective person to be represented, by word, circular, letter, or by advertisement. The department may impose a monetary penalty on the representative, and if the representative was acting on behalf of an employer or any firm or other entity in connection with the conduct giving rise to the penalty, the department may impose a monetary penalty on the employer, firm, or entity if it knew, or reasonably should have known, of the conduct. The penalty may not exceed the ***gross*** income derived, or to

be derived, from the conduct giving rise to the penalty and may be in addition to, or instead of, suspension, disbarment, or censure of the representative. . . .

(Emphasis added.)

85. **S.C. Code Ann. § 12-62-50**
Code of Laws of South Carolina 1976 Annotated
Title 12. Taxation
Chapter 62. South Carolina Motion Picture Incentive Act
§ 12-62-50. Tax rebate for employment of persons subject to South Carolina income tax withholdings.

. . .

(C) A motion picture production company claiming a rebate pursuant to this section, and all companies described in subsection (A)(2)(a)(ii) or (iii), must make payroll books and records available for inspection to the commission and the department at the times requested by the commission or the department. Each motion picture production company claiming the rebate, at the time of filing, must provide a report to both the commission and the department that includes the project's name, the name of each employee that worked on the motion picture, the social security number for each employee, the dates employed, the dates the employee worked on the motion picture, a job description for each employee, the total ***gross*** wages for each employee, the South Carolina taxable wages subject to withholding for each employee, the amount of rebate attributable to that employee, and other information considered necessary by the commission or the department. The report also must contain the total amount of withholding attributable to all employees that worked on the motion picture in South Carolina.

(Emphasis added.)

Exhibit W

1

Re-order from Bushnell Company
(215) 641-9520
www.BushnellCo.com

1350

STATE OF SOUTH CAROLINA

'C' CORPORATION INCOME TAX RETURN

Return is due on or before the 15th day of the 3rd month following the close of the taxable year.

If a refund or zero return, mail to: SC DOR, Corporate Refund, Columbia SC 29214-0032

If a balance due return, mail to: SC DOR, Corporate Taxable, Columbia SC 29214-0033

SC 1120

(Rev. 12/9/11)

3091

SC FILE # _____ - ____

INCOME TAX PERIOD ENDING _____

LICENSE FEE PERIOD ENDING _____

FEIN _____

NAME _____

MAILING ADDRESS _____

CITY _____ STATE _____ ZIP CODE _____

Change of ☐ Address ☐ Accounting Period ☐ Officers

Attach complete copy of Federal Return

County or Counties in SC Where Property is Located:

City **Audit Location** State

Audit Contact Telephone Number

Check if ☐ **Amended Return** ▶ ☐ **Consolidated Return** (Complete Schedule M)

☐ **Includes Disregarded LLC(s)** (Complete Schedule L)

Total Gross Receipts. ▶ | Total cost of depreciable personal property in SC. ▶

If Filing a Final Return, see General Instructions, page 6.
You MUST close your account with the SECRETARY OF STATE and complete I-349.
▶ ☐ Merged ☐ Reorganized ☐ Dissolved ☐ Withdrawn

PART I COMPUTATION OF INCOME TAX LIABILITY

1. Federal Taxable Income per federal tax return ▶ 1. _____
2. Net Adjustment from line 12, Schedule A and B 2. _____
3. Total Net Income as Reconciled (line 1 plus or minus line 2) ▶ 3. _____
4. If Multi-state Corporation, enter amount from line 6, Schedule G; otherwise, enter amount from line 3. ▶ 4. _____
5. LESS: South Carolina net operating loss carryover, if applicable 5. _____
6. South Carolina Net Income subject to tax (line 4 less line 5) ▶ 6. _____
7. TAX: Multiply amount on line 6 by 5% (.05) 7. _____
8. Less tax deferred on income from foreign trade receipts (see instructions) ▶ 8. _____
9. Balance (line 7 less line 8) 9. _____
10. Credit Carryover (line 7, Schedule C) ▶ _____ Non-refundable credits (line 5, Schedule C). ▶ 10. < _____ >
11. Balance of tax (line 9 less line 10). Enter the difference but not less than zero. 11. _____
12. Interest on DISC-deferred tax liability _____; or Foreign Trade Deferred Tax Liability _____ 12. _____
13. Total tax and/or interest (add lines 11 and 12) 13. _____
14. **Payments:** (a) Tax Withheld (Attach 1099s, I-290s, and/or W-2s; see instructions) ▶ _____
    (b) Paid by Declaration ▶ _____ (c) Paid with Tentative Return ▶ _____
    (d) Credit from Line 29b ▶ _____
    Refundable Credits: (e) Ammonia Additive ▶ _____ (f) Milk Credit ▶ _____
15. Total Payments and Refundable Credits (add lines 14a through 14f) 15. _____
16. Balance of Tax and/or Interest Due (line 13 less line 15) ▶ 16. _____
17. Interest Due ▶ _____ Penalty Due ▶ _____ (See penalty and interest instructions.) Enter Total. ▶ 17. _____
18. **TOTAL INCOME TAX**, Interest and Penalty Due (add lines 16 and 17) **BALANCE DUE** 18. _____
19. **OVERPAYMENT** (line 15 less line 13) _____ To be applied as follows:
    (a) Estimated Tax ▶ _____ **(b) License Fee** ▶ _____ **(c) REFUNDED** ▶ _____

PART II COMPUTATION OF LICENSE FEE

20. Total Capital And Paid In Surplus (Multi-State Corporations See Schedule E) ▶ 20. _____
21. FEE DUE - Line 20 x .001, plus $15.00 (**Fee cannot be less than $25.00 per taxpayer**) 21. _____
22. Credit Carryover ▶ _____ Credit taken this year from SC1120TC, Part II, Column C ▶ 22. < _____ >
23. Balance (line 21 less line 22) 23. _____
24. Payments: (24a) Paid with Tentative Return ▶ _____ (24b) Credit from line 19b ▶ _____
25. Total Payments (add line 24a and 24b) 25. _____
26. Balance of Fee Due (line 23 less line 25) ▶ 26. _____
27. Interest Due ▶ _____ Penalty Due ▶ _____ (See penalty and interest instructions.) Enter Total. ▶ 27. _____
28. **TOTAL LICENSE FEE**, Interest and Penalty Due (add lines 26 and 27) **BALANCE DUE** 28. _____
29. **OVERPAYMENT** (line 25 less line 23) _____ To be applied as follows:
    (a) Estimated Tax ▶ _____ **(b) Income Tax** ▶ _____ **(c) REFUNDED** ▶ _____
30. **GRAND TOTAL: INCOME TAX and LICENSE FEE DUE** (add lines 18 and 28) . . . EFT ☐ ▶ 30. _____

For Office Use Only

30911010

SCHEDULE A AND B ADDITIONS TO FEDERAL TAXABLE INCOME

1.	Taxes on or Measured By Income	1.	
2.	Federal Net Operating Loss	2.	
3.		3.	
4.		4.	
5.	Other Additions (attach schedule)	5.	
6.	Total Additions (add lines 1 through 5)		6.

DEDUCTIONS FROM FEDERAL TAXABLE INCOME

7.	Interest On Obligations Of The U.S.	7.	
8.		8.	
9.		9.	
10.	Other Deductions (attach schedule)	10.	
11.	Total Deductions (add lines 7 through 10)		11.
12.	Net Adjustment (line 6 less line 11) Also enter on line 2, Part 1, SC1120		12.

SCHEDULE C SUMMARY OF INCOME TAX CREDITS (FROM SC1120-TC)

1.	Credit Carryover From Previous Year's SC1120, Schedule C (NOTE: Should agree to SC1120-TC Column A, line 16)	1.	
2.	Enter Total Credits from SC1120-TC, Column B, line 16. **SC1120-TC must be attached to return.**	2.	
3.	Total Credits (add lines 1 and 2)	3.	
4.	Tax (line 9, Part 1, SC1120)	4.	
5.	Lesser of line 3 or 4 (enter on line 10, Part 1, SC1120) (NOTE: Should agree to SC1120-TC, Column C, line 16.)	5.	
6.	Enter Credits Lost Due to Statute (NOTE: Should agree to SC1120-TC, Column D, line 16.)	6.	
7.	Credit Carryover (line 3 less lines 5 and 6) (NOTE: Should agree to SC1120-TC, Column E, line 16.)	7.	

Please Sign Here I, the undersigned, a principal officer of the corporation for which this return is made declare that this return, including accompanying Annual Report, statements and schedules, has been examined by me and is to the best of my knowledge and belief, a true and complete return.

Signature of officer | Date | Title | Telephone Number

I **authorize** the Director of the Department of Revenue or delegate to discuss this return, attachments and related tax matters with the preparer. Yes ☐ No ☐ | Preparer's Printed Name

Paid Preparer's Use Only

Preparer's signature | Date | Check if self-employed ☐ | Preparer's Telephone Number

Firm's name (or yours if self-employed) and address | PTIN or FEIN | ZIP Code

If this is a corporation's final return, signing here authorizes the Department of Revenue to disclose that information with the Secretary of State. You must close with the Secretary of State as well as the Department of Revenue and complete I-349.

Taxpayer's Signature | Date

ATTACH COMPLETE COPY OF FEDERAL RETURN

Make check payable to: SC Department of Revenue. Include Business Name, FEIN and SC File Number. Go to www.sctax.org and look for the DOR ePay logo for other payment options.

30912018

SCHEDULE D **ANNUAL REPORT TO BE COMPLETED BY ALL CORPORATIONS**

1. Name _____
2. Incorporated under the laws of the State of _____
3. Location of the Registered Office of the Corporation in the State of South Carolina is _____
   In the City of _____ Registered Agent at such address is _____
4. Location of principal office (street address) _____
   Nature of principal business in SC _____
5. The total number of **authorized shares** of capital stock, itemized by class and series, if any, within each class is as follows:
   NUMBER OF SHARES: _____ CLASS: _____ SERIES: _____
6. The total number of **issued and outstanding shares** of capital stock itemized by class and series, if any, within each class is as follows:
   NUMBER OF SHARES: _____ CLASS: _____ SERIES: _____
7. The names and business addresses of the directors (or individuals functioning as directors) and principal officers in the Corporation are: (If additional space is necessary, attach separate schedule).

   NAME TITLE BUSINESS ADDRESS

   _____
   _____
   _____
   _____
   _____
   _____
8. Date Incorporated _____ Date commenced business in the State of South Carolina was _____
9. Date of this report _____ FEIN _____
10. If Foreign Corporation, the date qualified to do business in the State of South Carolina is _____
11. Was the name of the Corporation changed during the year? _____ Give old name _____
12. The Corporation's books are in the care of _____
    Located at (street address) _____
13. If filing consolidated, complete and attach Schedule J for each Corporation included in the consolidation.
14. The total amount of stated capital per balance sheet is:
    A. Total paid in Capital Stock (cannot be a negative amount) . . . . . $_____
    B. Total paid in Capital Surplus (cannot be a negative amount). . . . . $_____
    C. Total amount of stated Capital (cannot be a negative amount) . . . . . $_____

	1. Property Within South Carolina		2. Total Property Everywhere	
	(a) Beginning Period	(b) Ending Period	(a) Beginning Period	(b) Ending Period
1. Land				
2. Buildings				
3. Machinery and Equipment				
4. Inventories				
5. Other Property				
6. Exclusions	< >	< >	< >	< >
7. TOTAL (add lines 1 - 5; subtract line 6)				

30913016

ONLY MULTI-STATE CORPORATIONS MUST COMPLETE SCHEDULES E, F, G, AND H

SCHEDULE E COMPUTATION OF LICENSE FEE OF MULTI-STATE CORPORATIONS

1. Total Capital and Paid-in-Surplus at end of Year. . . . . $ _____
2. SC PROPORTION: (line 1 X ratio from Schedule H-1, H-2 or H-3, as appropriate). Also enter on line 20, Part II . . . $ _____

SCHEDULE F INCOME SUBJECT TO DIRECT ALLOCATION

	Gross Amounts 1	Less: Related Expenses 2	Net Amounts Allocated Direct. to SC and Other States 3	Net Amounts Allocated Directly to SC 4	Payrolls to be Excluded from Payroll Factor 5	Property to be Excluded from Property Factor 6
1. Interest not connected with business						
2. Dividends received						
3. Rents						
4. Gains/losses on real property						
5. Gains/losses on intangible pers. prop.						
6. Investment income directly allocated						
7. TOTAL INCOME DIRECTLY ALLOCATED						
8. INCOME DIRECTLY ALLOCATED TO SC						
9. TOTALS TO APPORTIONMENT FACTORS						

SCHEDULE G COMPUTATION OF TAXABLE INCOME OF MULTI-STATE CORPORATIONS

1. Total net income as reconciled. Enter amount from line 3, Page 1. . . . . 1. _____
2. Less: Income subject to direct allocation to SC and other states from Schedule F, line 7 . . . . . 2. _____
3. Total net income subject to apportionment (line 1 less line 2) . . . . . 3. _____
4. Multiply amount on line 3 by appropriate ratio from Schedule H-1, H-2, or H-3 and enter result here . . . . . 4. _____
5. Add: Income subject to direct allocation to SC from Schedule F, line 8 . . . . . 5. _____
6. Total SC Net Income (sum of lines 4 and 5 above) also enter on line 4, Part 1 of Page 1 . . . . . 6. _____

SCHEDULE H-1 COMPUTATION OF SALES RATIO

	Amount	Ratio
1. Total Sales Within South Carolina (see instructions)		
2. Total Sales Everywhere (see instructions)		
3. Sales Ratio (line 1 ÷ line 2)		%

Note: If there are no sales anywhere: Enter 100% on Line 3, if South Carolina is the principal place of business OR
Enter 0% on Line 3, if principal place of business is outside South Carolina.

SCHEDULE H-2 COMPUTATION OF GROSS RECEIPTS RATIO

	Amount	Ratio
1. South Carolina Gross Receipts		
2. Amounts Allocated to South Carolina on Schedule F	< >	
3. South Carolina Adjusted Gross Receipts (line 1 – line 2)		
4. Total Gross Receipts		
5. Total Amounts Allocated on Schedule F	< >	
6. Total Adjusted Gross Receipts (line 4 – line 5)		
7. Gross Receipts Ratio (line 3 ÷ line 6)		%

SCHEDULE H-3 COMPUTATION OF RATIO FOR SECTION 12-6-2310 COMPANIES

	Amount	Ratio
1. Total Within South Carolina (see instructions)		
2. Total Everywhere		
3. Taxable Ratio (line 1 ÷ line 2)		%

30914014

SCHEDULE I **RESERVED**

SCHEDULE J **CORPORATIONS INCLUDED IN CONSOLIDATED RETURN**
AFFILIATED CORPORATION NO.____

1. Name _____
2. Incorporated under the laws of the State of _____
3. Location of the Registered Office of the Corporation in the State of South Carolina is _____
   In the City of _____ Registered Agent at such address is _____
4. Location of principal office (street address) _____
   Nature of principal business in S.C. _____
5. The total number of **authorized shares** of capital stock, itemized by class and series, if any, within each class is as follows:

NUMBER OF SHARES	CLASS	SERIES

6. The total number of **issued and outstanding shares** of capital stock itemized by class and series, if any, within each class is as follows:

NUMBER OF SHARES	CLASS	SERIES

7. The names and business addresses of the directors (or individuals functioning as directors) and principal officers in the Corporation are: (If additional space is necessary, attach separate schedule).

NAME	TITLE	BUSINESS ADDRESS

8. Date Incorporated _____ Date commenced business in the State of South Carolina was _____
9. Date of this report _____ FEIN _____ SC File # _____
10. If Foreign Corporation, the date qualified to do business in the State of South Carolina is _____
11. Was the name of the Corporation changed during the year?_____ Give old name _____
12. The Corporation's books are in the care of _____
    Located at (street address) _____
13. Corporate Mailing Address _____
14. The total amount of stated capital per balance sheet is:
    A. Total paid in Capital Stock (cannot be a negative amount) . . . . . $_____
    B. Total paid in Capital Surplus (cannot be a negative amount) . . . . . $_____
    C. Total amount of stated Capital (cannot be a negative amount) . . . . . $_____

For additional affiliated corporations, include additional Schedule Js as needed.

30915012

SCHEDULE L **DISREGARDED LLCs INCLUDED IN RETURN**

A. If one or more Limited Liability Companies (LLCs) are included, list South Carolina LLCs only.

Name	FEIN	SC File No. (if applicable)

Include additional Schedule Ls as needed.

ATTACH COMPLETE COPY OF FEDERAL RETURN

Make check payable to: SC Department of Revenue. Include Business Name, FEIN and SC File Number. Go to www.sctax.org and look for the DOR ePay logo for other payment options.

39016019

SCHEDULE M CONSOLIDATED RETURN AFFILIATIONS SCHEDULE

Include additional Schedule Ms as needed. Include only corporations doing business in SC.

Part 1 General Information

Is the Common Parent Corporation included in the return?

Yes ☐ No ☐

If NO, enter Name and Federal Employer Identification Number (FEIN) of Common Parent Corporation.

NAME OF COMMON PARENT CORPORATION _____ FEIN _____

Name of Each Corporation Included in This Consolidated Return	FEIN
Corporation 1	
Corporation 2	
Corporation 3	
Corporation 4	
Corporation 5	
Corporation 6	
Corporation 7	
Corporation 8	

Part 2 Income Tax Information

	Federal Taxable Income	Amounts Directly Allocated	Amounts Allocated to SC	SC Adjustments	SC NOL Prior Year Carryovers
Corporation 1	$	$	$	$	$
Corporation 2					
Corporation 3					
Corporation 4					
Corporation 5					
Corporation 6					
Corporation 7					
Corporation 8					
Total	Equals page 1, line 1	Equals Sch. F, line 7	Equals Sch. F, line 8	Equals page 1, line 2	Equals page 1, line 5

Part 3 License Fee, Allocation, and Apportionment Information

	Tax Credited on Return	Total Capital and Paid in Surplus	Apportionment Percentage	License Fee
Corporation 1	$	$	%	$
Corporation 2				
Corporation 3				
Corporation 4				
Corporation 5				
Corporation 6				
Corporation 7				
Corporation 8				
Total	Equals page 1, line 14	Equals page 1, line 20	Per Schedule H	Equals page 1, line 21

39017017



Re-order from Bushnell Company
(215) 542-0520
www.BushnellCo.com

1350

TAX YEAR 2012

STATE OF SOUTH CAROLINA
DEPARTMENT OF REVENUE

PROPERTY RETURN

PT-300
(Rev. 1/20/11)
7012

▶ SID NUMBER _____ COUNTY _____ ▶ Office Use Only

▶ RETURN FILING STATUS: (check one)

☐ 1 Initial ☐ 2 Annual ☐ 3 Amended ☐ 4 Final ☐ 5 Return Due to Change in Accounting Closing Period

OWNER NAME AND MAILING ADDRESS

Report name and address corrections below. Ownership changes should be reported in the Change in Ownership section.

ATTN: _____
Name _____
Street _____
City, State, ZIP _____

ACCOUNT DATA

FEIN or SS No. _____
Property Location
Street _____
City _____ ZIP _____
Phone No. _____
Accounting Closing Date _____ (Month/Year)
Start Up Date _____ (Month/Day/Year)
Contact Person _____
Contact Person Phone No. _____
Name Used to File Income Tax _____

Report changes, corrections and omissions below.

FEIN or SS No. _____
Property Location
Street _____
City _____ ZIP _____
Phone No. (_____) _____
Accounting Closing Date _____ (Month/Year)
Start Up Date _____ (Month/Day/Year)
Contact Person _____
Contact Person Phone No. (_____) _____

CHANGE IN OWNERSHIP (See application for exemption page 2)

☐ Facility Sold To: _____ FEIN/SSN _____
☐ Facility Purchased From: _____ FEIN/SSN _____
Street _____
City _____ State _____ ZIP _____
Date of Sale _____ Contact Person _____ Phone Number (_____) _____

SCHEDULE SUMMARY (Enter TOTAL GROSS COST below from PLANT/OPERATION Schedules A through F, S and T.)

SCHEDULE LETTER	SCHEDULE NUMBER	PLANT/OPERATION NAME	TOTAL GROSS COST

▶ ADDITIONAL SCHEDULES (Check if the following schedules are attached.)

☐ Schedule X Improvement Schedule
☐ Schedule Z Lease Schedule

See page 2 for required signature.

70121025

Our records indicate the following leases are associated with your account. All additional leases should be reported on Schedule Z.

Mail to:

South Carolina Department of Revenue
Manufacturing Section
Columbia, SC 29214-0302

APPLICATION FOR FIVE YEAR PARTIAL EXEMPTION

Change In Ownership: The purchaser of an existing facility is required to obtain approval for exemption from the local county governing body for the five year partial exemption in accordance with SC Code section 12-37-220(C). A properly executed Department of Revenue form PT-444 must be furnished to the Department of Revenue within the time prescribed by law for the filing of an application for exemption. Forms are available on the website: www.sctax.org

No Change In Ownership: Owners of existing facilities that have not been purchased within this reporting period are not required to obtain approval from the local county governing body. The filing of the PT-300 with appropriated schedules within the time prescribed by law for filing of application for exemption is deemed to be the application for the partial exemption under SC Code sections 12-37-220(A)(7), (A)(8), (B)(32) and (B)(34).

APPLICATION FOR SPECIAL ASSESSMENT OF WAREHOUSING (PT-465)

Taxpayers are required to file form PT-465 with the Property Division of SCDOR by July 1st of the tax year requesting the special classification. See SC Code Sections 12-43-220 (a)(4) and form PT-465 for qualifications and application procedures.

Section 12-54-44 (B)(I) A person who wilfully attempts in any manner to evade or defeat a tax or property assessment imposed by a title administered by the department or the payment of that tax or property assessement, in addition to other penalties provided by law, is guilty of a felony and, upon conviction, must be fined not more than ten thousand dollars or imprisoned not more than five years, or both, together with the cost of prosecution.

I declare that this return, including any accompanying schedules and statements, has been examined by me and to the best of my knowledge and belief is a true and complete return reflecting gross capitalized costs and net book values, if applicable, as used for income tax, made in good faith pursuant to the provisions of the Code of Laws, and amendments.

TAXPAYER:		PREPARED BY:	
Please print		Please print	
Signature		Signature	
Date	Phone Number	Date	Phone Number

All returns must be signed and dated by the preparer and the taxpayer or an officer of the company.

70122023

Exhibit X

RECYCLED PAPER
RECYCLABLE

Brief of Appellant

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SCDOR022372

QUESTIONS

1. Did the lower court err in limiting the application of § 12-19-110 solely to customer changes and thereby precluding from taxation the receipts derived from the sale of the nuclear facility?

2. Does § 12-19-110, as applied to the respondent, violate the Equal Protection Clauses of the South Carolina and United States Constitutions?

3. Did the lower court err in awarding costs to the respondent?

SCDOR022373

STATEMENT

The matter before the court arises out of a transaction whereby the respondent sold to various parties a portion of its nuclear generating facility located in York County, South Carolina. The appellant took the position that the gross receipts derived from this sale should be included within the respondent's tax base for purposes of calculating its corporate license tax liability under § 12-19-110. The respondent excepted to such and the matter proceeded to the lower court.

At the lower court there was a disagreement as to what issues were actually raised by the respondent's Complaint.[1] It would now appear that this disagreement is irrelevant in that the lower court's decision was based solely on an issue that was properly before it. Since the respondent prevailed on this particular point, the court found it unnecessary to address the other issues. (See Tr., p. 24.)

The substance of the lower court's decision was that § 12-19-110 was limited to imposing a license tax on receipts from customer charges. (See Tr., p. 24.) Accordingly, the court determined the receipts from the sale

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[1] See the Statement (Tr., pp. 2 and 3), the respondent's Complaint (Tr., pp. 6 and 7) and the appellant's Exceptions #15 and #16 (Tr., pp. 27 and 28).

of the nuclear facility should not be included in the respondent's license tax base.

The appeal now before this court presents two major issues. The first is whether § 12-19-110 is limited in its application to customer charges thus precluding from taxation the receipts derived from the sale of the nuclear facility.

The second issue is raised by the respondent's additional sustaining ground. That issue is whether § 12-19-110 is unconstitutional under the Equal Protection Clauses of the State and Federal Constitutions.[2]

A lesser issue is also presented regarding the lower court awarding costs to the respondent. That issue is simply whether such an award was proper.

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[2]Although properly before the lower court, this issue was one that the court declined to address.

ARGUMENT

I

THE LOWER COURT ERRED IN LIMITING THE APPLICATION OF § 12-19-110 SOLELY TO CUSTOMER CHARGES AND THEREBY PRECLUDING FROM TAXATION THE RECEIPTS DERIVED FROM THE SALE OF THE NUCLEAR FACILITY. (Exceptions 1, 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 17 and 18)

Chapter 19 of Title 12 sets forth a taxing scheme that imposes a franchise tax upon the privilege of doing business as a corporation in South Carolina. United States Rubber Co. v. Query, 19 F.Supp. 191 (1937). Included within that Chapter are §§ 12-19-100 and 12-19-110, both of which levy a license tax on regulated corporations such as the respondent. In the instant situation, it is the provisions of § 12-19-110 that are in question. During the relevant tax year,[3] those provisions provided as follows:

> "In addition to the license fee provided by § 12-19-100 and any and all other license taxes and fees or taxes of whatever kind, there is hereby levied an annual license fee of three mills upon the entire gross receipts from business within this State during the calendar year next preceding by every railroad company, express company, street railway company, navigation company, waterworks company, power company, distribution electric cooperative, light company, gas company, telegraph company, telephone company, parlor, dining or sleeping car company, tank car company, refrigerating car company, fruit growers' express car company, and all other privately operated car lines. The license fee provided for by this section shall be paid at the time of filing the reports required by this chapter.

[3] Section 12-19-110 was amended in 1985.

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> Electric cooperatives subject to the license fee imposed by § 12-19-100 and distribution electric cooperatives subject to the license fee provided by this section shall file reports pursuant to the provisions of §§ 12-19-20 and 12-19-130. Provided, however, that the first report of electric cooperatives, together with the payment of the fee, shall be made between March 15, 1970 and June 30, 1970." (Emphasis added)

The above language clearly indicates that the license tax on corporations, such as the respondent, is based on entire gross receipts and not just receipts from customer charges. Accordingly, the lower court's attempt to apply such a limitation here was improper. Where a statute is clear and unambiguous, there is no room for construction and the terms of the statute must be given their literal meaning. Southeastern Fire Ins. Co. v. South Carolina Tax Commission, 253 S.C. 407, 171 S.E.2d 355 (1969); Green v. Zimmerman, 269 S.C. 535, 238 S.E.2d 323 (1977).

The broad import of the words "entire gross receipts" was not lost on the Ohio Supreme Court in Sandusky Gas and Electric Co. v. State, 114 O.S. 479, 151 N.E. 685, 71 A.L.R. 260 (1926). When reviewing a statute similar to § 12-19-110, the court there commented that a tax based on such words would go beyond customer charges.

> "The levy of an excise tax upon the gross receipts of public utility companies is made pursuant to the provisions of sections 5417, 5474, 5475, and 5483, General Code, and the words 'entire gross receipts,' as there employed, mean and include the entire

> receipts of such company from the intrastate business done by it, under the exercise of its corporate powers, whether from the operation of the utility itself or from any other business done by it."

Moreover, contrary to the lower court's conclusion, the language "from business in this state" does not necessarily limit § 12-19-110's application to customer charges. This is similar to the argument made by the taxpayer in State v. United Electric Light & Water Co., 90 Ct. 452, 97 A. 857 (1916). There, Connecticut levied a corporation license tax on gross earnings from operations in that state. The taxpayer attempted to exclude from such tax the earnings received from the sale of various residual products by claiming that the only earnings subject to taxation were those earnings received by it from the sale of electricity to its customers. The court rejected this argument by noting that the statutory language of the tax statute was broad enough to include gross earnings from all sources.

Although there is no South Carolina case law directly on point, it should be noted that for purposes of allocating and apportioning income, the word "business" has been interpreted as including income derived from the sale of property connected with a taxpayer's business. In Texaco, Inc. v. Wasson, 269 S.C. 255, 237 S.E.2d 75 (1977), the court held that royalties received by Texaco from its sulfur and salt mines in Texas must be apportioned to South

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Carolina because such were derived from properties connected with Texaco's oil business.

The appellant's Regulation 117-89.1 also requires that the receipts from the sale of the nuclear facility should be included within the measure of the tax levied by § 12-19-110. That Regulation states:

> "Gross receipts, as used in § 12-19-110 of the South Carolina Income Tax Act of 1926, as amended, shall include all receipts from operations within the State, and also other profit and loss items with a local situs. Intangible income from intangibles used in the conduct of the business within this State shall be included in gross receipts."

This Regulation, along with the appellant's Finding (Tr., p. 12), demonstrate that the appellant has long interpreted § 12-19-110 as applying to more than the mere receipts from customer charges. Such a construction of § 12-19-110, by the agency charged with executing it, is entitled to the most respectful consideration and should not be overruled without cogent reasons. Faile v. S. C. Employment Security Commission, 267 S.C. 536, 230 S.E.2d 219 (1976); Stephenson Finance Company v. South Carolina Tax Commission, 242 S.C. 98, 130 S.E.2d 72 (1963).

Additionally, the fact that Tax Regulation 117-89.1 makes reference to "other profit and loss items" does not imply that the appellant interprets § 12-19-110 as being limited to taxing the gain on the sale of an asset.

The appellant's Finding clearly states that such term "is used to identify certain items and does not relate to the manner of taxation". (Tr., p. 13) In this instance, such would identify the nuclear facility.

It is also noteworthy that § 12-19-110 was amended in 1985. A review of this amended version and an application of the rules of statutory construction lend support to the appellant's position that prior to its amendment § 12-19-110 was not limited to customer charges. The relevant provision of § 12-19-110 now reads:

> "In addition to the license fee provided by § 12-19-100 and any and all other license taxes and fees or taxes of whatever kind, there is levied an annual license fee of three mills upon the gross receipts derived from services rendered from regulated business within this State during the calendar year next preceding by every railroad company, express company, street railway company, navigation company, waterworks company, power company, distribution electric cooperative, light company, gas company, telegraph company, telephone company, parlor, dining or sleeping car company, tank car company, refrigerating car company, fruit growers' express car company, and all other privately operated car line. * * *."

The new language of § 12-19-110 now states that the tax levied therein is restricted to "receipts derived from services rendered". This indicates that the prior language of § 12-19-110 was not limited in this respect. Where the General Assembly has adopted an amendment to a

statute, it is presumed that it intended to change the existing law. Vernon v. Harleyville Mutual Casuality Company, 244 S.C. 152, 135 S.E.2d 841 (1964); North River Insurance Company v. Gibson, 244 S.C. 393, 137 S.E.2d 264 (1964).

For the most part, the lower court relied upon the original enactment of § 12-19-110[4] to arrive at its decision. The court reasoned that the use of the word "operations" therein indicated that the corporate license tax is limited to customer charges. This reasoning is incorrect for two reasons.

First, a reading of that Act in its entirety reveals that the term "gross earnings from operations" applies only to railroads. Section 1 of the Act requires various corporations to report differing items of information to the Comptroller General for purposes of levying the subject tax. At subsection 12 of § 1, it is stated that each railroad must report the "gross earnings from its operation". On the other hand, subsection 13 of that same section requires power companies such as Duke to report their "entire gross receipts". From that point on, all regulated corporations, to include railroads and power companies, are addressed together in the same sections with the phrases "gross earnings from operations" and "entire

[4]See Act No. 269, Acts of 1904.

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gross receipts" both appearing therein. It stands to reason that each of these phrases must be applied only to those corporations to which they relate. To do otherwise would make the reporting system of § 1 of no value. It must be remembered that in construing legislation, it is a rule that the General Assembly did not intend to do a futile thing. Gaffney v. Mallory, 186 S.C. 337, 195 S.E. 840 (1938); McLeod v. Montgomery, 244 S.C. 308, 136 S.E.2d 778 (1964).

Second, even if the word "operation" does apply to utilities, such does not necessarily imply that the tax here is restricted to customer charges. As previously stated, the court in State v. United Electric Light and Water Co., supra, refused to apply such an interpretation even though the tax there was levied "on gross earnings from operations" (emphasis added). Similarly, the appellant's Finding also points out that "operations" usually relate to the whole process of planning for and operating a business. Liller v. Logsdon, 261 Md. 367, 275 A.2d 469 (1971). In view of such, it is foreseeable that the operations of a corporation would include the buying and selling of assets either used or anticipated for use by that corporation in the conduct of its business.

Finally, the appellant's interpretation of § 12-19-110 does not lead to absurd results.[5] There is

[5] See the lower court's Order at Tr., p. 21.

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nothing in the record to indicate that the appellant would consider both the principal and interest of a redeemed bond as being gross receipts under § 12-19-110. In point of fact, the appellant's own Regulation, 117-89.1, shows a different result. It states that "Intangible income from intangibles used in the conduct of the business within this state shall be included in gross receipts", thus inferring the appellant would only consider the income of the bond as gross receipts. A similar result would also be reached with regard to any loans made by the respondent.

Likewise, the appellant's interpretation of § 12-19-110 does not have the effect of taxing the same subject matter twice.[6] The subject matter of the tax levied by § 12-19-110 is gross receipts while that of § 12-19-100 is the fair market value of all property owned by a corporation such as the respondent. This same situation arises with telephone companies. They are also subject to both §§ 12-19-100 and 12-19-110. Naturally, any receipts received from the sale or renting of telephones would be included within the measure of the tax levied by § 12-19-110, while at the same time the fair market value of such phones would be included within § 12-19-100.

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[6]See the lower court's Order at Tr., p. 22.

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ARGUMENT

II

SECTION 12-19-110, AS APPLIED TO THE RESPONDENT, DOES NOT VIOLATE THE EQUAL PROTECTION CLAUSES OF THE SOUTH CAROLINA AND UNITED STATES CONSTITUTIONS. (Respondent's Additional Sustaining Ground)

The respondent raises the additional sustaining ground that § 12-19-110 is unconstitutional under the Equal Protection Clauses of the Federal and State Constitutions. As a basis for such, the respondent argued before the lower court that utilities have to pay more license tax than other corporations thus creating an unconstitutional situation.

The fact the respondent is classified differently than certain other corporations and must pay a higher license tax as a result of this classification does not necessarily indicate that § 12-19-110 is unconstitutional. It is a basic fundamental of taxation that the Equal Protection Clause does not prohibit states from drawing lines that treat one class of taxpayers differently from others. Lehnhausen v. Lake Shore Auto Parts Co., 410 U.S. 356, 93 S.Ct. 1001 (1973). This principle applies likewise to corporations. 71 Am.Jur.2d, State and Local Taxation, § 186, p. 505.

In the instant situation, the General Assembly has chosen to divide all corporations into two classes for purposes of levying its corporate license tax. The first class is unregulated corporations[7] while the second of

[7] See § 12-19-70 for the tax rate imposed on this class.

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which the respondent is a member, is composed of those corporations regulated by the South Carolina Public Service Commission. Such a classification scheme is presumed constitutional with the burden being on the respondent to show that there is no conceivable basis supporting the same.

> " * * *. There is a presumption of constitutionality which can be overcome 'only by the most explicit demonstration that a classification is a hostile and oppressive discrimination against particular persons and classes.' * * *. 'The burden is on the one attacking the legislative arrangement to negative every conceivable basis which might support it.' * * *." Lehnhausen v. Lake Shore Auto Parts Co, supra.

> "An ordinance is a legislative enactment and is presumed to be constitutional. The burden is upon the taxpayer to prove unconstitutionality beyond a reasonable doubt. The burden requires the attacker to ' . . . negative every conceivable basis which might support it.'" North Charleston Land Corp. v. The City of North Charleston, et al., South Carolina Supreme Court's Opinion No. 22079, April 9, 1984.

Moreover, the courts have long recognized that there is a rational basis for taxing regulated corporations at a higher rate than unregulated corporations. In so doing, they have justified such upon the grounds that these corporations enjoy the right of eminent domain, exercises relative freedom from competition and have other advantages over the general business community. New York Rapid Transit Corp. v. City of New York, 303 U.S. 573, 82 L.Ed. 1024, 58

S.Ct. 721, reh. den., 304 U.S. 588, 82 L.Ed. 1548, 58 S.Ct. 939 (1938); New York Steam Corp. v. New York, 268 N.Y. 137, 197 N.E. 172, 172 A.L.R. 1157 (1935). A review of Title 57 of the South Carolina Code of Laws indicates that corporations such as the respondent receive similar benefits.[8]

Contrary to the argument made by the respondent before the lower court, Southern Bell Tel. & Tel. Co. v. City of Aiken, 279 S.C. 269, 306 S.E.2d 220 (1983), is not applicable. In that case, the taxpayer was taxed at 24 times the average rate. Although the lower court there upheld the ordinance imposing this tax, the matter was reversed on appeal because the lower court's Order failed to state a rational basis for taxing the taxpayer at a higher rate.

Here, unlike the situation in Southern Bell Tel. & Tel. Co., not only is there a rational basis for supporting the classification in question but the respondent itself has failed to meet its burden of proof. All the respondent has done is allege that it pays more taxes under § 12-19-110 than it would if it were paying taxes under § 12-19-70. Certainly, this does not meet the burden of negating every conceivable basis which might support South Carolina's corporate license tax classification scheme.

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[8] See for example § 58-27-130 (condemnation powers) and § 58-27-1230 (limiting establishment of new utilities).

ARGUMENT
III

THE LOWER COURT ERRED IN AWARDING COSTS TO THE RESPONDENT. (Exception 19)

Pursuant to Rule 54(d), South Carolina Rules of Civil Procedure, costs against the appellant can be imposed only to the extent provided for by law. In the instant situation, the respondent's action was brought under § 12-47-440. (Tr., pp. 1 and 2) As to those remedies found in Chapter 47 of Title 12, § 12-47-270 controls the awarding of costs.[9] That provision states:

> "In any action brought under the provisions of § 12-47-220 or 12-47- 230, no costs or disbursements shall be taxed or allowed in favor of either party, except for the service of process and procuring the attendance of witnesses."

The above indicates that costs are only appropriate when actions are brought under § 12-47-220 or § 12-47-230. Inasmuch as the action here is by way of § 12-47-440, the awarding of costs was improper.

However, even if § 12-47-270 could be construed as applying to § 12-47-440, the costs recoverable would be limited to those for service of process and the procurement of witnesses. Pendarvis v. S. C. Tax Commission, Davis Advance Sheets, Opinion No. 2239. This would afford the

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[9] None of the remedies found in Chapter 47 of Title 12 provide for costs. It is only by way of § 12-47-270 that such is afforded.

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respondent very little since there were no witnesses (Tr., p. 15) and the cost of service was minimal.

CONCLUSION

It is respectfully submitted that the Order of the lower court should be reversed and the proceeds derived from the sale of the nuclear facility included within the respondent's corporate license tax base. Such is premised upon the language of § 12-19-110, Tax Regulation 89-1, the rules of statutory construction and relevant case law.

It is additionally submitted that § 12-19-110 does not violate the Equal Protection provisions of either the Federal or State Constitutions. As shown above, there is a rational basis for taxing the respondent at a higher rate.

Finally, the lower court erred in awarding costs to the respondent. An award of costs against a state agency is permissible only when provided for by law. Here the law does not make such a provision.

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CERTIFICATE OF SERVICE BY MAIL

I, Ronald W. Urban, hereby certify that I have mailed, postage prepaid, three copies of the Brief of Appellant in re Duke Power Company v. South Carolina Tax Commission, Case No. 86-344, to William E. Booth, III, Esq., Griffith, Mays, Foster & Kittrell, 2512 Devine Street, Columbia, South Carolina 29205, this 12 day of June, 1986.

Ronald W. Urban

RONALD W. URBAN
Assistant Attorney General

RECEIVED
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Brief of Respondent

COUNTER-STATEMENT OF QUESTIONS PRESENTED

I. Whether under S.C. Code §12-47-110 (1976) (before a 1985 amendment), corporate annual license fees of almost $900,000 were lawfully and legally imposed on a corporation engaged in the business of generating, transmitting and distributing electrical power in this State in view of the fact that the fees were assessed on proceeds received by the electrical utility from the sale of a portion of a partially constructed nuclear power plant for which the utility received a minimal amount above its actual costs?

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STATEMENT OF FACTS

This is an action under S.C. Code §12-47-440 (1976) for the recovery of corporate license fees paid by Respondent, Duke Power Company ("Duke"), a North Carolina corporation engaged in the business of generating, transmitting and distributing electrical power in both North and South Carolina (Tr. 1). The Circuit Judge, the Honorable David F. McInnis, ordered the Appellant, South Carolina Tax Commission ("Commission"), to refund Duke the sum of $1,143,863 with interest as allowed by law.

This action arose from an assessment made by the Commission on July 12, 1984, assessing Duke for additional fees and interest for the 1982 corporate license fee tax year. The additional liability arising from the assessment was as follows:

License Tax	$ 886,722.00
Interest	257,141.00
TOTAL	$ 1,143,863.00

(Tr. 10)[1]

During 1981, Duke consummated the sale of a partial interest in a nuclear power plant and its support facilities which are located in York County, South Carolina (Tr. 1).

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[1]References are to page numbers in the Transcript of Record.

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At the time of sale, the Catawba Nuclear Station was under construction and had not produced any electrical power (Tr. 16). While Duke received proceeds in excess of one half billion dollars from the sale, the amount received by Duke in excess of its actual costs was minimal (Tr. 13).

Duke did not report any of the proceeds received from the sale of the unfinished Catawba Nuclear Station on the tax return for the payment of its 1982 corporate license fees. The only gross receipts reported on the return were from customer charges for the furnishing of electrical power (Tr. 9-10). After an audit by the Field Services Division of the Commission, Duke was notified that a proposed assessment of additional license fees would be considered by the Commission. The proposed assessment was based upon the amount attributable to the sale of real property and improvements related to the Catawba Nuclear Station situated in the State of South Carolina (Tr. 10). This amount was $295,205,499 on which the license fee of three mills was assessed by the Commission under S.C. Code §12-19-110 (1976). Duke paid the additional assessment on July 31, 1984,[2] without protest.

After payment of the assessment, Duke requested a conference before the Commission to consider Duke's objections to the additional assessment. After the conference, a

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[2]The Circuit Court's Order incorrectly states that the payment was made on July 31, 1985. The parties have agreed in the Statement that the correct year of payment was 1984 (Tr. 3).

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Finding was issued by the Commission on May 17, 1985, rejecting all objections made by Duke and affirming the proposed assessment made by the Field Services Division. On June 20, 1985, §12-19-110 was amended by the Legislature expressly limiting its scope to gross receipts derived from services rendered.[3]

On June 14, 1985, Duke filed an application under S.C. Code §12-47-440 (1976), for refund of the additional assessment, and was subsequently notified by the Commission that the application had been denied (Tr. 5-6). On September 26, 1985, Duke commenced this action upon the filing and service of a summons and complaint. The Commission filed an Answer attaching a copy of its Finding issued on May 17, 1985, and the action was tried as a non-jury case on February 6, 1986, before Judge McInnis in the Court of Common Pleas for Richland County.

After considering the pleadings, oral arguments and briefs of the parties, Judge McInnis was convinced that the Commission misinterpreted §12-19-110 prior to the 1985 amendment. The Circuit Court held that §12-19-110 was limited in its scope to the imposition of license fees on receipts from customer charges for the regulated business of an electrical utility.

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[3]§41 of Act No. 9 of the 1985 Acts and Joint Resolutions.

ARGUMENT

I. Under S.C. Code §12-47-110 (1976) (before a 1985 amendment), corporate annual license fees of almost $900,000 were unlawfully and illegally imposed on a corporation engaged in the business of generating, transmitting and distributing electrical power in this State in view of the fact that the fees were assessed on proceeds received by the electrical utility from the sale of a portion of a partially constructed nuclear power plant for which the utility received a minimal amount above its actual costs. (Question I.)

The facts surrounding this action are undisputed. The essential fact is that the assessment for additional corporate license fees paid by Duke was based upon a portion of the proceeds received from the sale of an unfinished nuclear power station. The Catawba Nuclear Station, at the time of the sale, had not produced any electricity for customers of Duke.

At the time of the assessment, Duke was required to pay annually a license fee of (1) one mill upon each dollar of the fair market value of its property (§12-19-100), and (2) three mills upon "the entire gross receipts from business within this State" (§12-19-110). One month after the

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Commission issued its Finding that a portion of the proceeds received by Duke from the sale of the unfinished Catawba Nuclear Station was subject to the corporate license fee tax, the Legislature amended §12-19-110 to read, in pertinent part, as follows:

> "In addition to the license fee provided by §12-19-100 and any and all other license taxes and fees or taxes of whatever kind, there is levied an annual license fee of three mills upon the gross receipts derived from services rendered from regulated business within this State . . . ."

(emphasis on added language).

The Circuit Court gave six (6) separate reasons for being convinced that the Commission had misinterpreted the scope of §12-19-110 prior to the 1985 amendment. Those reasons as summarized are as follows:

1. The construction borne by the original enactment of §12-19-110 indicates that the license fee tax was only to be imposed on gross receipts from customers of a utility.

2. The selling of a partially constructed generating facility does not constitute business done by an electrical utility.

3. An absurd result can be illustrated from the Commission's interpretation of §12-19-110.

4. Commission Regulation 117-89.1 limits the scope of §12-19-110.

5. An electrical utility pays annual license fees based on the value of its property under another statute and such property was not intended to be taxed again under §12-19-110.

6. The 1985 amendment to §12-19-110 was intended to change the Commission's interpretation of that statute.

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The concept of assessing an annual license fee on regulated businesses for the privilege of carrying on business in this State based on their volume of business was introduced in 1904. The pertinent portion of the original enactment of §12-19-110 is as follows:

> "That the said State Board of Assessors shall, after ascertaining the gross receipts for business done in South Carolina, or the gross receipts from its operations within South Carolina of any . . . power company . . . notify the State Treasurer of the amount thereof on or before the first day of May of each year, and the State Treasurer shall thereupon proceed to charge and collect from such company and such company shall pay to said State Treasurer an annual license fee of three mills on the gross income of such company for business done within South Carolina for the preceding fiscal year . . ."
>
> Section 9 of Act No. 269 of the 1904 Acts and Joint Resolutions.

The measure of taxation under the original enactment of §12-19-110 specifically included gross receipts from its operations as well as gross receipts for business done. The phrase "gross receipts from its operations" was eliminated in a 1953 amendment.[4] The previous existence of that phrase was found by the Circuit Court to indicate that the Legislature intended for license fees to be assessed only upon gross receipts from customers of an electrical utility for the furnishing of electrical service.

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[4]Act No. 48 of the 1953 Acts and Joint Resolutions.

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The construction borne by the original statute must be considered when determining the meaning of a statute. South Carolina Elec., etc. v. Public Serv., 272 S.C. 316, 251 S.E.2d 753 (1979). In determining that the time computation under S.C. Code §15-1-20 (1976) was only applicable to civil cases and not applicable to administrative law cases, the Supreme Court found controlling the fact that the original enactment of §15-1-20 contained the phrase "as herein provided". Id., 251 S.E.2d at 756. The Court found that the subsequent elimination of that phrase was intended only to clarify the law without changing the meaning borne by the original enactment. In that case, the Supreme Court stated the following:

> "The revised or consolidated statute will be construed as bearing the same meaning as the original statute or section unless the language of the revision or consolidation plainly requires a change of construction to conform to the manifest intent of the Legislature."

Id., 251 S.E.2d at 756.

The Commission argues, however, that assuming the eliminated phrase limits the scope of §12-19-110 to customer receipts, other sections of the original enactment dealing with reporting requirements indicate that the eliminated language was only applicable to railroad companies. Brief of Appellant at 9. No reason is given by the Commission as to why the Legislature would have intended for the scope of

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§12-19-110 to be different in the case of railroad companies. Obviously, there is no logical reason for railroad companies to be taxed differently from other businesses subject to §12-19-110. This is evident from the fact that the 1953 amendment did not eliminate railroad companies from the application of the volume measured license fee tax. Even Commission Regulation 117-89.1, adopted prior to 1936,[5] defines gross receipts as including "all receipts from operations within the State" and is applicable to all companies subject to the volume measured license fee tax.

The language of the statutory scheme used in the State of Washington for imposing excise taxes upon various regulated businesses has also changed. At one time, the excise tax was imposed on gross operating revenues. Later, the statute was amended so that the tax was measured by the gross income of the regulated business. The Court of Appeals of Washington held that this change in phraseology was not material and "the definition of these two terms (gross operating revenues vs. gross income) are identical." The City of Seattle v. The State, 12 Wash.App. 91, 527 P.2d 1404, 1406 (n.3) (1974).

In a previous case, the Supreme Court of Washington held that revenues received by a water district as reimbur-

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[5]The Regulation refers to §12-19-110 of the 1926 Code of Laws and the next codification of the Code of Laws was in 1936.

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sement for the cost of constructing, installing, and inspecting new facilities necessary to operate a water distribution system to serve prospective customers were not gross operating revenues subject to the excise tax. King County Water Dist. 68 v. Tax Commission, 362 P.2d 244 (Wash. 1941). "Gross operating revenue" was defined by statute as meaning the value proceeding or accruing from the performance of the particular public service or transportation business involved, including operations incidental thereto. Id. at 245.

Similarly, the proceeds from the sale of a partially constructed nuclear generating facility are not operating revenues accruing from the performance of the business of generating, transmitting, and distributing electrical power. Although this State has no statutory definition of gross receipts, the definition found in the State of Washington is clearly reasonable considering the purpose and intent of a volume measured license fee tax. A tax statute must be construed reasonably as a whole with the view of carrying out its purpose and intent. Hay v. Leonard, 212 S.C. 81, 46 S.E.2d 653 (1948). As stated in that case,

> "'where the language relied upon to bring the particular person or subject within the law is ambiguous or is reasonably susceptible of an interpretation that would exclude the person or subject sought to be taxed, the well-established general rule requires that any substantial doubt should be resolved against the government and in favor of the taxpayer.'"

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Id., 46 S.E.2d at 245; accord, Commonwealth Natural Resources, Inc. v. Com., 219 Va. 529, 248 S.E.2d 791, 796 (1978).

The case relied upon by the Commission as to the meaning of "operations" defines that word as being the whole process of planning for and operating a business or other organized unit. Liller v. Logsdon, 261 Md. 367, 275 A.2d 469 (1971). The issue in Liller was whether mining operations had ceased terminating certain easement rights. In the instant case, revenues or receipts from operations of Duke constitute consideration received for electricity distributed, supplied, furnished or sold to persons for use or consumption. It is not foreseeable that the operations of an electrical utility would include the selling of generating facilities used or anticipated for use by that utility in the conduct of its business. Such a course or procedure of productive activity would actually be unproductive since the assets sold produce the product sold by the utility.

Likewise, the word "business" in §12-19-110 indicates that the proceeds from the sale of a generating facility by an electrical utility are not subject to the license fee tax. The business of Duke is generating, transmitting, and distributing electrical power to its customers. S.C. Code §58-27-10 (1976). This presupposes the existence of electrical generating facilities to operate. See, King

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County Water District No. 68 v. Tax Commission, supra at 245. The construction of the Catawba Nuclear Station cannot constitute operations of such a facility. Again, an electrical utility is in the business of operating generating facilities not selling them. Duke could not continue to carry on its business very long if it regularly sold its electrical generating facilities. This would be contrary to the legal obligation of Duke to provide electrical service to its customers within its service area. Clearly, therefore, the proceeds from the sale of a generating facility are not gross receipts accruing from the performance of the business done by an electrical utility.

The gross receipts received by a telephone company for the rental of telephone poles by other utilities are not subject to the franchise tax imposed by the State of North Carolina. Southern Bell Telephone & Telegraph Co. v. Clayton, 266 N.C. 687, 147 S.E.2d 195 (1966). The term gross receipts was defined by statute as follows:

> "Such gross receipts shall include all rentals, other similar charges, and all tolls received from business which both originates and terminates in the State of North Carolina, whether such business in the course of transmission goes outside of the State or not . . ."

Id., 147 S.E.2d at 196.

The Supreme Court of North Carolina looked at the purpose of the franchise tax and the fact that telephone

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companies are not engaged in the business of renting either real estate or utility poles in affirming the lower court's order requiring the Commissioner of Revenue to refund the franchise taxes imposed on the receipts from such rentals. The count stated the following:

> "Such rentals, when they occur, are purely incidental arrangements. The income of a telephone company comes from service charges for the transmission of messages by telephones which remain the property of the company."

Id., 147 S.E.2d at 197.

In conclusion, the court stated the obvious. The scope of a tax imposed on a regulated company for the privilege of engaging in business is limited to receipts obtained from the services the utility is obligated to furnish the public unless the statute specifically defines gross receipts as being "from any and all sources whatsoever except those expressly exempted." Id., 147 S.E. at 198. The North Carolina statute applicable to electrical utilities is identical in substance to §12-19-110 prior to the 1985 amendment, and imposes a franchise tax on gross receipts from business done by the utility. N.C. G.S. §105-116.

The 1916 case of State v. United Electric Light and Power Company, 90 Ct. 452, 97 A. 857, is distinguishable. In that case, a company, apparently as a regular part of its business operations, sold apples grown upon its land and ice

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produced from its ponds. Duke does not, as a regular part of its business operations, sell its electrical generating facilities.

The case of Sandusky Gas and Electric Co. v. State, 114 Ohio St. 479, 151 N.E. 685 (1926), is also distinguishable. The court, in that case, defined gross receipts as receipts from business done by the company, whether from the operation of the utility itself or from any other business done by it. The utility failed to report, as gross receipts, the sums paid by it to a natural gas supplier claiming it was engaged in a joint enterprise with the supplier. It had purchased the gas from the supplier and distributed it through its main lines for sale to its customers. Only the amount received from its customers in excess of the price paid to the supplier was reported on the utility's excise tax returns for the tax years in question. The principal issue involved in that case was whether the excise tax should be apportioned between the two utilities. The Supreme Court of Ohio held that under the circumstances no joint enterprise existed. Id., 151 N.E.2d at 687.

Patently, the Sandusky Gas and Electric Co. case involved revenues obtained from services the utility was obligated to furnish the public; i.e. gross receipts from business done by the utility. Moreover, a subsequent Ohio judicial decision refused to extend the scope of the excise

tax to include receipts from the sale of merchandise and electrical appliances by a utility company. Haefner v. City of Youngstown, 147 Ohio St. 58, 68 N.E.2d 64 (1946). It is evident, therefore, that the Ohio Supreme Court would hold that excise taxes cannot be imposed on the proceeds from the sale of a generating facility by an electrical utility.

Moreover, there is no doubt that the broad definition used by the Commission for the measure of tax under §12-19-110 prior to the 1985 amendment will produce absurd results. The imposition of tax under §12-19-110 as construed by the Commission does not appear to have any exceptions. The repayment of loans made by an electrical utility or the liquidation of a short-term investment would produce receipts for the utility. An electrical utility may loan money to an employee or sell the employee safety equipment at cost. An electrical utility will often make a short-term investment of funds not needed for the operation of its business. The receipts from those sources should be subject to taxation under the Commission's interpretation of the scope of §12-19-110. However, to impose taxation in such cases would be absurd. A Court will reject the plain and ordinary meaning of the words in a statute when to accept it would lead to a result so plainly absurd that it would not possibly have been intended by the Legislature. Boyd v. State Farm Mutual Automobile Insurance Co., 260 S.C.

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386, 195 S.E.2d 706 (1973); 73 Am.Jur.2d, Statutes (1974).

In addition, the broad interpretation given by the Commission to §12-19-110 prior to the 1985 amendment is inconsistent with its own regulations. Regulation 117-89.1 provides as follows:

> "Gross receipts, as used in Section 12-19-110 of the South Carolina Income Tax Act of 1926, as amended, shall include all receipts from operations within the State, and also other profit and loss items with a local situs. Intangible income from intangibles used in the conduct of the business within this State shall be included in gross receipts."

While the above Regulation is extremely unclear, the Circuit Court interpreted its language as indicating that the measure of taxation for the sale of property is the gain, if any. Such an interpretation would avoid the unfairness and absurdity resulting from the imposition of the license fee tax on the entire receipts from the repayment of loans or the sale of safety equipment at cost. In the instant case, only a minimal amount of fees would have been imposed under the interpretation given the above Regulation by the Circuit Court since Duke sold a portion of the Catawba Nuclear Station for almost its costs. Nevertheless, the Regulation is invalid as to imposing any license fees on the proceeds from the sale of assets by an electrical utility because the underlying statute does not impose fees in such cases. See, Heyward v. South Carolina

Tax Commission, 240 S.C. 347, 126 S.E.2d 15 (1962).

As a fifth reason for concluding that the Commission had misinterpreted §12-19-110 prior to the 1985 amendment, the Circuit Court found that the property of an electrical utility was taxed under §12-19-100. The annual license fee under that Section is based upon the fair market value of the utility's property. Since both of these statutes were enacted at the same time, the imposition of a license fee tax twice upon the same subject matter could not have been intended by the Legislature.

The final reason given by the Circuit Court for its decision was based on the 1985 amendment to §12-19-110. There is no doubt that the present language of §12-19-110 does not impose a license fee tax on the proceeds of the sale of an asset by an electrical utility. The Commission concedes this result. Brief of Appellant at 8.

The Commission contends that 1985 amendment was intended to change the existing law. However, the general rule is that the adoption of an amendment which materially changes the terminology of a statute only raises a presumption that the amendment was intended to change the existing law. North River Insurance Company v. Gibson, 244 S.C. 393, 137 S.E.2d 264 (1964). As stated in North River Insurance Company v. Gibson, "like all rules of construction, the presumption is merely an aid in interpreting an

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ambiguous statute and determining the legislative intent". Id., 137 S.E.2d at 266.

Another rule of statutory construction allows a court to look at the circumstances regarding the enactment of the law. As stated in Greenville Baseball v. Bearden, 200 S.C. 363, 20 S.E.2d 813, 816 (1942), "the history of the period in which the Act was passed may be considered." In the instant case, a week after the Finding of the Commission was issued and almost two years from the date of the assessment, the Legislature changed the law. The Circuit Court viewed the quick reaction of the Legislature to change the Commission's interpretation of §12-19-100 as evidence that the Legislature did not agree with the Commission's interpretation. Clearly, therefore, the presumption that the 1985 amendment was intended to change existing law is refuted upon consideration of the circumstances surrounding the enactment of the 1985 amendment.

CONCLUSION

For the reasons stated in this Brief, the Respondent respectfully requests that this Court affirm the Circuit Court's Order requiring the South Carolina Tax Commission to refund to Duke $1,143,863 plus interest.

Respectfully submitted,

William E. Booth III
Attorney for the Respondent

July 14, 1986

SCDOR022408

I, William E. Booth III, hereby certify that I have mailed, postage prepaid, three (3) copies of the Brief of Respondent in re: Duke Power Company v. South Carolina Tax Commission, Case No. 86-344, to Ronald W. Urban, Esquire, Assistant Attorney General, Post Office Box 125, Columbia, South Carolina 29214, this 14th day of July, 1986.

William E. Booth III
Attorney for Respondent

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SCDOR022409

Exhibit Y

1



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2002 WL 34271923 (Ill.Cir.)

Circuit Court of Illinois,
County Department - Law Division.
Cook County
THE MEAD CORPORATION, an Ohio Corporation, Plaintiff,
v.
ILLINOIS DEPARTMENT OF REVENUE, Glen L. Bower, Director of Revenue, and Judy Baar Topinka, Treasurer of the State of Illinois, Defendants.
No. 00 CH 07854.
February, 2002.

Order

Alexander P. White, Judge.
This matter is before the Court on Plaintiff's and Defendant's cross motions for Partial Summary Judgment. The Court finds:
1. Plaintiff's request for Partial Summary Judgment states that the Illinois Statutes require the inclusion of gross receipts on the sale of investments in the denominator of Mead's sales factor.
2. Defendant's cross motion for Partial Summary Judgment states that the Illinois Statutes, together with applicable regulations, require the inclusion of net gain on the sale of investments in the denominator of Mead's sales factor.

The Court finds that the composition of the sales factor is set forth in 35 ILCS 5/1501 (a) (3) (A):
The sales factor is a fraction, in the numerator of which is the total sales of the person in this State during the taxable year, and the denominator of which is the total sales of the person everywhere during the taxable year.

The term "sales" is defined in 35 ILCS 5/1501 (a) (21) as "all gross receipts of the taxpayer not allocated under Section 301, 302, and 303." The income from sales of financial instruments is further defined in 86 Ill. Adm. Code Section 100.3380 (c) (5) (B) where those financial instruments are merely held. In the instant case, there was active management. Thus, 86 Ill. Adm. Code Section 100.3380 (c) (5) (B) does not apply. Furthermore, 86 Ill. Adm. Code Section 100.3380 (c) (6), which describes how income from investments in intangibles merely held are characterized in the determination of business income, is not applicable.

It is hereby ordered that Plaintiff's Partial Summary Judgment is granted, and Defendant's Partial Summary Judgment is denied.

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JUDGE Alexander P. White

The Mead Corp. v. Illinois Dept. of Revenue
2002 WL 34271923 (Ill.Cir.) (Trial Order)

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Rhode Island State Tax Reporter, Western Electric Co., Inc. v. John H. Norberg, Tax Administrator, District Court (Rhode Island), ¶200-145, (Mar. 30, 1983)

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Western Electric Co., Inc. v. John H. Norberg, Tax Administrator

¶200-145. District Court (Rhode Island), A. A. No. 81-391, 461 A.2d 679, March 30, 1983.

Certiorari denied, Supreme Court of Rhode Island, No. 83-286-M.P, June 23, 1983

Franchise: Corporation Income: Apportionment of Income: Corporations Doing Business Interstate: Gross Receipts: Short-Term Securities: Second Apportionment Fraction: Prior Law.– In determining the apportionment of the taxpayer's income to Rhode Island, the taxpayer properly included all receipts from the sale of short-term securities in its computation. In order to find the correct apportionment to the state, the mean of three fractions had to be taken and applied to the taxpayer's total income wherever derived. During the contested period, the total gross receipts from the sale of the securities had to be included in the denominator of the second fraction of the apportionment formula. The Tax Administrator claimed that only the net gains and interest from the sale of the securities should have been included, and the principal or basis should not have been included. The Administrator claimed that including the gross receipts distorted the apportionment formula. Even though the legislature saw fit to amend the statute to comport with the Tax Administrator's contention, the amendment was not applicable to tax years ending before June 30, 1982. Thus, the tax periods contested by the taxpayer ended before the amendment became effective. The plain language of the statute before the amendment required that the total gross receipts be included in the apportionment formula. Accordingly, the decision of the Tax Administrator was reversed and the taxpayer was entitled to a refund. G. L., Sec. 44-11-14.

Ed. Note: Sec. 44-11-14, G. L., was amended by Ch. 291, Laws 1982. The amendment required that only the net income from the sale of securities be included in the second apportionment fraction.

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1985 WL 19912 (Wis.Tax.App.Com.)

Tax Appeals Commission
State of Wisconsin

*1 UNITED STATES STEEL CORPORATION, PETITIONER
600 Grant Street
Pittsburgh,
PA 15230
v.
WISCONSIN DEPARTMENT OF REVENUE, RESPONDENT
P.O. Box 8933
Madison, WI 53708

Docket No. I–6578

May 9, 1985

DECISION AND ORDER

(Drafted by Commissioner Doyle)

The above-entitled matter having come on to be heard by this Commission; the petitioner, United States Steel Corporation, having appeared by its attorneys, Foley & Lardner, by Thomas G. Ragatz and Leonard S. Sosnowski; the respondent, Wisconsin Department of Revenue, having appeared by its attorney, Irving F. Shapiro; having considered the entire record herein, this Commission hereby finds, decides and orders as follows:

FINDINGS OF FACT

1. On August 24, 1977, respondent issued to petitioner a Notice of Assessment of Additional Franchise Tax and Notice of Action on Claim for Refund for the calendar years 1972–1975, indicating the total additional tax and interest due to be $663,520.41.

2. By letter dated September 22, 1977, petitioner petitioned for redetermination of the respondent's Assessment of Additional Franchise Tax and Partial Denial of Claim for Refund. As part of petitioner's said petition for redetermination, petitioner made an additional Claim for Refund as to franchise taxes paid which petitioner claimed were not properly owing for the year 1975 relating to the addition of intangible income to Wisconsin apportionable income.

3. By notice dated October 7, 1977, respondent denied petitioner's additional Claim for Refund.

4. By letter dated October 18, 1977, petitioner petitioned for redetermination of respondent's denial of petitioner's additional Claim for Refund.

5. By notice dated April 28, 1978, respondent granted in part and denied in part petitioner's petitions for redetermination resulting from respondent's additional assessment and respondent's denials of petitioner's claims for refunds for

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the years at issue herein.

6. This is a timely appeal to this Commission from respondent's actions on petitioner's petitions for redetermination.

(The following Findings of Fact relate to the years 1972–1975, unless otherwise indicated)

7. Petitioner is a Delaware corporation, with its main corporate headquarters in Pittsburgh and New York. It has commercial domicile in Pennsylvania.

8. Petitioner is a multi-state, multi-national corporation doing business in all but one of the United States and numerous foreign countries.

9. There are five major segments comprising petitioner's domestic operations; each segment is made up of several divisions. The five major segments are as follows: manufacture and sale of steel; fabricating and engineering; chemicals; transportation; and cement.

10. In addition to the above segments, petitioner has other miscellaneous operations, including USS Realty Development ('Realty'), Sterling Park Development Division ('Sterling Park'), and the New York Investment Division ('Investment Division'). These operations are conducted as divisions of petitioner and are not subsidiary corporations.

*2 11. Petitioner owns the following subsidiaries: twelve railroad subsidiaries; Orinco Mining Company; U.S. Steel International; United States Steel International Sales Co. (DISC); Intupersa; Navigen Company; and Navios Corporation.

12. Petitioner is a stockholder with less than a controlling interest in the following dividend paying corporations; Ashco, Inc.; Oglebay Norton Company; Rinker Materials Co.; Structural Dynamics Research Corporation; and Altos Hornos de Vizcaya, S.A.

13. The five divisions of petitioner operating in Wisconsin during the relevant period were: (1) USS Division—production and sales of steel; (2) USS Supply Division—warehouses for sale of steel products; (3) USS Chemicals Division—manufacture of various industrial chemicals; (4) Universal Atlas Division—production and sale of cement products; and (5) USS Agri-Chemicals Division—manufacture of various nitrogen phosphatic fertilizer products.

14. Petitioner is not asserting herein that its income relating to the activities of four of its major segments as set forth in Paragraph 9., above, (manufacture and sale of steel; fabrication and engineering; chemicals; and cement) is not subject to apportionment in Wisconsin in that each of these divisions had activities in Wisconsin during the years at issue. It is petitioner's contention on the unitary issue that its transportation operation is not part of its unitary business in Wisconsin because this activity is carried out through subsidiaries which did no business in Wisconsin. In addition, petitioner is contending that three of its divisions, Realty, Sterling Park and Investment Division, were not part of its unitary business in Wisconsin.

15. Petitioner raises the following issues in addition to the above-stated contention on the unitary issue, in its objection to respondent's actions herein:

(1) Whether respondent's method of determining apportionable income relating to its mining operations was arbitrary, in violation of the principle of the Wisconsin statutory three factor approach to apportionment, and/or in violation of the statutory pattern in sec. 71.07, Wis. Stats., for determining apportionable income by shifting further emphasis in the formula to sales and away from property and payroll;

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(2) Whether respondent erred in including petitioner's intangible income in apportionable income;

(3) Whether all intangible proceeds from the sales, exchanges and redemptions of intangible assets should be included in petitioner's gross receipts for the purpose of calculating the denominator of the sales factor on petitioner's 1975 return;

(4) Whether the property, payroll and sales of petitioner's dividend paying subsidiaries should have been included in the denominators of the property, payroll and sales factors for purposes of calculating intangible income apportionable to Wisconsin;

(5) Whether Wisconsin's double weighted sales factor results in attributing to Wisconsin income out of all appropriate proportion to the activities of petitioner in Wisconsin; results in multiple state taxation or results in attributing to Wisconsin, for taxation, income on Wisconsin destination sales which has already been taxed in the state where the manufacturing was performed; and/or results in a discrimination against interstate commerce; and

*3 (6) Whether the increase in the relative tax burdens on petitioner from the law changes incorporating destination sales, double weighted sales and intangible income into the apportionment calculation constitutes a burden on inter-state commerce, and/or whether this increased burden has any rational relationship to the activities of petitioner in Wisconsin.

16. Each division of petitioner is run as a separate profit unit, operating under the principle of 'functional profitability independence'. Each division has a separate set of books and records and a separate profit and loss statement. Each division is headed by an executive officer, hired and fired by petitioner's top level management. Each division determines how best to accomplish its goal of making a profit, with each unit having responsibility for getting a rate of return competitive with what outside businesses in the same line are earning.

17. Each division has its own sales, advertising, personnel, accounting, etc., departments. However, the division may rely on petitioner's central office to provide assistance in purchasing, accounting, personnel, legal matters, tax problems, etc. There is no requirement that the divisions utilize these services (they may go outside), and the divisions are charged for these services at market rates. These charges are taken against the division's profit and loss statement. Intra-company transactions are conducted at arm's length.

18. Certain services of the central office benefit the entire company, e.g., lobbying on environmental or labor matters, public relations, pension and employee insurance plans, corporate-wide self-insured coverage, labor negotiations, transportation planning, safety practices, planning for future facilities, economic studies, centralized and uniform accounting system, research and development, central computer system, and advertising of a corporate image type. Petitioner's central tax department is responsible for preparation of tax returns, state and federal. Each division is responsible for preparation of its own financial statements, which are submitted to the central office for consolidation for SEC reporting and the annual report. On occasion, petitioner's employees are transferred between divisions for further experience training. The steel and raw materials divisions are coordinated to a great extent through the central office. Petitioner has a Vice-President Accounting-Other Divisions whose responsibility is to work with divisions other than steel and raw materials to make sure that petitioner has the coordination and uniformity necessary to carry out its programs and policies.

19. If a division is in need of funds for expansion, the head of the division would look to petitioner's Treasurer, and advances made to a division in excess of its budget would be subject to the discretion of top management.

20. The head of each division is responsible for preparation on an annual basis of a forecast of profits and losses, a budget and expected rate of return, plus a projection for the next three years, which is reviewed with the next higher

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level of management. These budgets and forecasts are submitted to the central accounting office for preparation of a company-wide projection, which is approved by petitioner's Corporate Policy Committee.

*4 21. Petitioner's Board of Directors establishes the overall policies for petitioner and approves certain activities, e.g., filings with the Securities and Exchange Commission, the annual report, major expenditures of the corporation and its dividend policy.

22. The Corporate Policy Committee is a committee of the Board of Directors whose principal function is carrying out certain policies designated by the Board. It also acts as the primary approval group before going to the Board, and in some cases, the Board has delegated to this committee authority for approval of certain financial matters.

23. The Corporate Management Committee is a committee of the Board of Directors whose principal functions are to review the profit and loss results of the divisions, and to review the operating situations of each division. Through this committee, each division keeps top management advised of the status of its business, reporting its results and where it stands in relation to its expectations for the year, and discussing the problems it might be having.

24. All excess cash of the divisions not needed for day-to-day operations is turned over to the Investment Division, where it is co-mingled with other business receipts and invested at the discretion of the New York investment staff. Once these funds are co-mingled, it is impossible to trace the source of the funds.

25. If funds are needed by petitioner's management for expansion, capital acquisitions or acquisitions of new businesses, needed funds are obtained either through borrowing, the corporate treasury, or sales of stock. The decision as to the source of financing is made by top management with approval of the Corporate Policy Committee.

26. The Investment Division has been in existence since at least the 1930's. Its offices are located in petitioner's New York headquarters. This Division is under the supervision of the corporate treasurer. Although because of the nature of this operation it has had little need of petitioner's central services, the Investment Division operates in relation to petitioner's central office in a similar manner to petitioner's other divisions, see Paragraphs 16.–25., above.

27. The main responsibility of the Investment Division is the management and investment of the cash of petitioner not needed for the day-to-day operations. The Investment Division is a sizable contributor to petitioner's income; in fact, the top money making division of petitioner in 1975.

28. The Investment Division is one of petitioner's regular business functions.

29. The Investment Division invests petitioner's excess cash in short-term investments (less than 1 1/2 years). These short-term investments are primarily in Treasury Bills, Notes and Bonds; Bankers Acceptances and Bankers Participation Certificates; Certificates of Deposits from various banks; commercial paper; and Canadian time deposits. Most of these short-term investments are negotiable instruments and are readily traded and sold by the Division.

*5 30. In 1975, the net income from intangibles earned through investments by the Investment Division was $303,871,292.

31. The Investment Division had one $20,000 Certificate of Deposit in Wisconsin, which was in the North Milwaukee State Bank, from which petitioner derived $1100 annual interest income. Other than this Certificate of Deposit, the Investment Division had no activity in Wisconsin; no securities kept in Wisconsin; no other bank accounts in Wisconsin; and no funds transferred for use in Wisconsin.

32. The Investment Division provides needed cash flow to other divisions of petitioner. Normally, the funds can be

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made available on short notice for use by other divisions or by petitioner for acquisitions. When the Investment Division is called upon the provide cash for another corporate purpose, it is for a specific purpose, such as working capital or a loan to a division, as specified through the Pittsburgh office. The Investment Division does provide cash for loans to subsidiaries which are interest bearing notes, usually tied to the prime rate.

33. Realty was created in 1969 with an initial capital investment from petitioner. The head of this division reports to the Vice-President of Realty and Finance. The purpose of Realty is to develop and manage corporate property to the best financial advantage, for corporate use and otherwise. It is construction oriented, having constructed shopping centers, industrial parks, warehouses and recreational facilities (e.g., theme hotels for Disney World). Realty constructs warehouses for lease to petitioner at market rental rates. On a few occasions, Realty has taken over facilities abandoned by petitioner.

34. Realty operates in relation to petitioner's central office in a similar manner to petitioner's other divisions, see Paragraphs 16.–25., above. Realty has its own accounting department, financial statements, and management. Realty uses outside engineers because it employs people from the community in which it is operating. Realty does not use petitioner's central research and development facilities, engineering department, advertising, labor services or legal counsel (although on a few occasions, it has used the legal services, paying for the service). Realty does have charges included in the Deductions listed on its Operating Statements for 1972–1975 (although not specifically delineated herein) for services provided by other administrative groups of petitioner. Realty has used petitioner's products in its construction activities.

35. Realty usually obtains financing by borrowing on the outside but has sought financial assistance from petitioner. Requests for additional funding are made by Realty's management through the appropriate channels within petitioner. The decision is made by petitioner's management whether to finance through petitioner or go outside.

36. Realty's excess earnings flow to petitioner, which takes control over these funds for use within the discretion of petitioner's management.

*6 37. Realty's accounting personnel are located in petitioner's Pittsburgh office building. Other employees of Realty are located throughout the United States. The paychecks are from the USS Realty Division payroll account.

38. Sterling Park was responsible for a housing development in Sterling Park, Virginia, consisting of single- and multi-family housing which were sold to the general public. It also developed and maintains a shopping center in the area. Prior to 1972, Sterling Park was a subsidiary of petitioner and was then changed into a division. It remains a very small division of petitioner. Sterling Park operates in relation to petitioner's central office in a similar manner to petitioner's other divisions, see Paragraphs 16.–25., above.

39. This division developed a warehouse for lease to petitioner's products division in Birmingham, Alabama, which was leased on the basis of commercial prices.

40. The head of Sterling Park reports to the Vice-President of Realty and Finance.

41. Neither Realty nor Sterling Park owns any land in Wisconsin and neither has any operations in Wisconsin.

42. Petitioner owns the following twelve domestic railroad subsidiaries:
Bessmer & Lake Erie Railroad Co.
Birmingham Southern Railroad Co.
Carbon County Railway Co.
Connelsville & Monongahela Railway Co.
Duluth, Missabe & Iron Range Railway Co.

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Elgin, Joliet and Eastern Railway Co.
Johnstown and Stony Creek Rail Road Co.
Lake Terminal Railroad Co.
McKeesport Connecting Railroad Co.
Newburgh and South Shore Railway Co.
Union Railroad Co.
Youngstown & Northern Railroad Co.

43. Petitioner did not organize any of these railroad companies but acquired existing companies around 1901, when petitioner corporation was organized. These twelve subsidiaries constitute one of the largest carrier systems in the United States in terms of profits. Petitioner holds a 100% interest in each of these companies, except for some of the preferred stock of Bessmer & Lake Erie Railroad Co.

44. In 1975, these railroad companies had approximately $500 million in assets. They owned 2700 miles of track, 445 locomotives, 32,000 freight cars and had 32,000 employees.

45. These railroad companies are common carriers, authorized to do business by the Interstate Commerce Commission ('ICC') and by various state regulatory agencies. Each company has its own Board of Directors, officers and employees. The companies have common directors and officers (with permission of the ICC), but have no common directors or officers with petitioner.

46. Petitioner plays no role in management of these companies and would be prohibited from doing so under the ICC. Petitioner merely acts as a shareholder in these companies, and as such, elects the Boards of the companies.

47. Each railroad has its own management, financing (each has its own credit line; petitioner does not participate in raising capital for any of these companies), and personnel benefits. Its employees are covered under the Railroad Retirement Act and the Railroad Unemployment Act, rather than Social Security and state unemployment plans. There are no common benefits for the employees of the railroad subsidiaries and petitioner's employees. These companies receive no management services from petitioner, and they do not look to petitioner or major policy decisions.

*7 48. The only capital contribution by petitioner to any of these companies was in 1978 to help finance a new facility for one of the companies.

49. The ICC requires that these companies remain independent. The ICC sets the rates charged by railroads, sets policies concerning abandonment, and requires a uniform accounting system. These companies are prohibited by law from discriminating in favor of any customer and actively seek customers other than petitioner.

50. Petitioner has opposed rate increases for railroads. Petitioner also uses other carriers, such as Conrail. However, a significant amount of the transactions of these railroads involve petitioner as the customer (the percentage of sales by the railroads to petitioner ranges from 39% to 100% of the railroads' total sales). These transactions are at market rates.

51. Each company, by its Board of Directors, determines its own dividend after examining the financial situation in a year. Petitioner has no input into that decision.

52. In determining the amount of income from petitioner's mining operations subject to apportionment, respondent's assessment separated net income from mining sales to third parties from total income from mining by using the ratio of sales to third parties to total income from mining, which methodology only considered sales and did not consider the property or payroll involved in the mining function.

53. Use of the statutory factors of sales, payroll and property to separate income from mining sales to third parties from

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total mining income shows a reduction in apportionable income of $9,885,876 in 1972, $11,591,610 in 1973, $19,763,010 in 1974, and $24,495,789 in 1975.

54. In computing the payroll and property factors for the apportionment formula, respondent used sales percentages to separate apportionable from non-apportionable payroll and property, which added to the overall impact of sales on the apportionment result.

55. Intupersa is a small steel fabricating plant located in Guatemala. It made no sales to petitioner and utilized local suppliers of raw materials and made all sales in that area. Petitioner owned 93% interest in this company. Petitioner may have had personnel on the Board, and the major policy decisions of Intupersa had to have approval of petitioner's Board of Directors.

56. Orinco Mining Company was a Venezuelan mining company which prior to 1975 was a supplier of iron ore to petitioner. Petitioner had a 100% interest in this company. In 1975, the Venezuelan government expropriated this company's property, as a result of which petitioner received a dividend of $115 million representing a return of petitioner's capital. Prior to January 1, 1975, petitioner had representatives on the Board of Orinco, but after January 1, 1975 the company no longer had any property. In 1975, this company sold its services to the Venezuelan government as mining consultants.

57. Navios Corporation and Navigen Company are two of petitioner's transportation subsidiaries. Petitioner had a 100% interest in both. They are both Liberian shipping lines. Navios did no business with petitioner in 1975. Navigen did provide ocean hauling services for petitioner in 1975, but on the same basis as transported for third parties. These companies had no common officers with petitioner and were operated independently and autonomously from petitioner.

*8 58. Petitioner presented no evidence concerning the operations of U.S. Steel International, Inc. and United States Steel International Sales Company (DISC) to show that these companies were discrete business enterprises.

59. In addition to its subsidiaries, petitioner owns a minority interest in the following dividend paying companies:
(1) Ashco, Inc.—engaged in pumping stations and water pipeline businesses—Petitioner owns a 35% interest in this company and has some input into its decisions.
(2) Oglebay Norton Co.—a large company on the New York Stock Exchange—Petitioner owns 3.4% interest in this company.
(3) Rinker Materials Co., Inc.—Petitioner owns an 11.29% interest in this company and has no input except as a shareholder.
(4) Structural Dynamics—Petitioner owns a 45% interest acquired with the proviso that Dr. Jason A. Lemon remain employed with this company for at least five years and that arrangements be made to protect petitioner's percentage of participation in the event that new stock is issued.
(5) Altos Hornos de Vizcaya, S.A.—a Spanish company in which petitioner has a 26.77% interest—Petitioner made a loan to this company in consideration for which petitioner was to have representation on the Board of Directors for ten years and at least 25% of the voting power of the stockholders, coupled with a change to be made in AHV's bylaws to assure that decisions be made only by a 76% vote—Also under the terms of the agreement, petitioner was to provide technical and managerial assistance for ten years.

60. As to the companies discussed in Paragraph 59., above, none of them had officers in common with petitioner, and there were no purchases or sales between these companies and petitioner. Petitioner has no legal control over these companies.

61. Petitioner's total sales in 1975 included its income from intangibles and the proceeds from the sale, exchange and redemption of intangible investments.

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62. There are no published statutory sections, Wisconsin Administrative Code sections, instruction booklets or other materials available to the public which set forth respondent's position as was stated in its internal Field Audit Section Bulletin 77–9 that only receipts from 'the main thrust of the taxpayer's business' are to be included in calculating the denominator of the sales factor. FASB 77–9 was not promulgated until 2 3/4 years after the 1975 statutory change as to intangible income became effective. Respondent had proposed an administrative rule which would have provided that for purposes of the calculation of the denominator of the sales factor, the term 'sales' only would include those 'from the taxpayer's principle business activity'. This rule was not enacted, on advice of counsel, because of the potential for problems in litigation.

63. Petitioner's total sales in 1975 included its income from intangibles and the proceeds from the sale, exchange and redemption of intangible investments.

CONCLUSIONS OF LAW

*9 1. Petitioner's USS Realty Development Division, Sterling Park Development Division and Investment Division were not discrete business enterprises but rather were integral parts of petitioner's unitary business during the period at issue. Under sec. 71.07(2), Wis. Stats., petitioner's business within Wisconsin was an integral part of such unitary business during the period at issue herein. Therefore, pursuant to sec. 71.07(2), Wis. Stats., petitioner's income derived from the operations of these divisions, including the intangible income derived from the operation of its Investment Division during 1975, was includable in its Wisconsin apportionable income for the years at issue.

2. Petitioner's twelve railroad subsidiaries were discrete business enterprises whose activities were unrelated to petitioner's activities in Wisconsin. Dividends received by petitioner from these subsidiaries are not properly includable in petitioner's Wisconsin apportionable income in 1975.

3. Petitioner's foreign subsidiaries, Orinco Mining Co., Intupersa, Navigen Company and Navios Corporation, were discrete business enterprises whose business activities were unrelated to petitioner's activities in Wisconsin. Dividends received by petitioner from these foreign subsidiaries are not properly includable in petitioner's Wisconsin apportionable income in 1975.

4. The following companies paying dividends to petitioner in 1975 were discrete business interprises whose business activities were unrelated to petitioner's activities in Wisconsin: Ashco, Inc.; Oglebay Norton Co.; Rinker Materials Co., Inc.; Structural Dynamics; and Altos Hornos de Vizcaya, S.A. Dividends received by petitioner from those foreign subsidiaries are not properly includable in petitioner's Wisconsin apportionable income in 1975.

5. Income from intangibles and proceeds from the sale, exchange and redemption of intangible investments received by petitioner in 1975 and includable in its 1975 Wisconsin apportionable income come within the intent and meaning of sec. 71.07(2)(c)1., Wis. Stats., as 'total sales' includable in the denominator of the sales factor.

6. Respondent's methodology in separating apportionable from non-apportionable income from petitioner's mining operations was in error in employing only a sales ratio to petitioner's total income from mining and was in error in using a sales ratio to determine apportionable payroll and property. Petitioner's methodology in determining Wisconsin apportionable income from mining, utilizing sales, property and payroll factors, was shown to be a more accurate calculation and is hereby adopted by the Commission. Respondent's determination of petitioner's Wisconsin apportionable income from mining operations is reduced as follows:

1972—reduced by $9,885,876;
1973—reduced by $11,591,610;
1974—reduced by $19,763,010;
1975—reduced by $24,495,789.

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7. Under Wisconsin law, petitioner is not entitled to combine the sales, payroll and property of dividend paying subsidiaries in the denominator of the three factors.

*10 8. The issues raised by petitioner in objecting to Wisconsin's imposition of the double weighted sales factor in conjunction with Wisconsin's change to destination based sales reporting and in objecting to the cumulative burden of Wisconsin taxation on petitioner's Wisconsin activities resulting from statutory changes (destination sales, double weighting the sales factor and inclusion of intangible income) are constitutional issues, and this Commission lacks authority or jurisdiction to rule on the constitutional issues raised by the petitioner.

Therefore,

IT IS ORDERED

That respondent's actions on petitioner's petitions for redetermination be modified to reflect the above Findings and Conclusions.

Dated at Madison, Wisconsin, this 9th day of May, 1985.

John P. Morris, Chairman
Thomas R. Timken, Commissioner
Catherine M. Doyle, Commissioner
William Bradford Smith, Commissioner
Mary K. Wagner-Malloy, Commissioner

OPINION

The petitioner, United States Steel Corporation, has raised a number of issues in this appeal as set forth in Findings of Fact, Paragraphs 14. and 15. The first issue raised by petitioner relates to the 'unitary business/formula apportionment' concept of allocating income to Wisconsin for taxation purposes, as provided for in sec. 71.07(2), Wis. Stats., as follows:

> (2) Corporation * * * engaged in business within and without the state shall be taxed only on such income as is derived from business transacted and property located within the state. The amount of such income attributable to Wisconsin may be determined by an allocation and separate accounting thereof, when the business of such corporation * * * within the state is not an integral part of a unitary business, but the department of revenue may permit an allocation and separate accounting in any case in which it is satisfied that the use of such method will properly reflect the income taxable by this state. (Emphasis added)

Petitioner contends that during period at issue herein, USS Realty Development, Sterling Park Development and Investment Division were each discrete business enterprises and were not part of petitioner's unitary business operating in Wisconsin. Petitioner contends that the income derived from these operations is therefore not properly includable in Wisconsin apportionable income for the years at issue.

A second, closely related, issue raised by petitioner is whether respondent erred in including petitioner's intangible income in the form of dividends and interest in petitioner's 1975 Wisconsin apportionable income. Effective July 31, 1975, sec. 71.07(1m), Wis. Stats., was created to read as follows:

> 71.07 Situs of Income; allocation and apportionment . . . (1m) CORPORATIONS. Income or loss from business, not requiring apportionment under sub. (2), (3) or (5), shall follow the situs of the business from which derived. Income or loss derived from rentals and royalties from real estate or tangible personal property, or from the operation of any farm, mine or quarry, or from the sale of real property or tangible personal property shall follow the

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situs of the property from which derived, except that gains or losses realized on disposals of real property or tangible personal property used in the production of business income shall follow the situs of the business. Income from personal services performed by employes of corporations, and from patents, copyrights, trademarks, tradenames, plans specifications, blueprints, processes, techniques, formulae, designs, layouts, patterns, drawings, manuals and technical know-how shall be deemed business income and shall follow the situs of the business. Gain or loss by a corporation on redemption of its own bonds shall be deemed business income or loss and shall follow the situs of the business, and a corporation's bond premium or discount shall be deemed business loss or income and shall follow the situs of the business, except that such income or loss of a personal holding company shall follow its residence. For purposes of this subsection, 'personal holding company' means 'personal holding company' as defined in section 542 of the internal revenue code in effect on December 31, 1974. Interest received on state and federal tax refunds when the tax refund was on business income or property shall be deemed income from business and shall follow the situs of the business from which derived.

*11 Following the enactment of sec. 71.07(1m), in those cases where income or loss from a business was subject to apportionment, respondent determined that intangible income must follow the situs of the business and be subject to apportionment.

Petitioner objects to the inclusion for 1975 of its intangible income in Wisconsin apportionable income on two grounds. Petitioner contends that its railroad subsidiaries (Findings of Fact, Paragraph 42.), its foreign subsidiaries (Findings of Fact, Paragraph 11., but not including U.S. Steel International and United States Steel International Sales Co. (DISC)), and dividend payors in which petitioner held a minority interest (Findings of Fact, Paragraph 12.) were each discrete business enterprises and were not part of petitioner's unitary business operating in Wisconsin. Based upon the same reasoning as for the first issue discussed above, petitioner argues that the income derived from these businesses is not properly includable in Wisconsin apportionable income for 1975.

Further, petitioner argues that even if the Commission should find that the Investment Division was part of petitioner's unitary business, under the holdings in two United States Supreme Court decisions, ASARCO Inc. v. Idaho State Tax Commission, 458 U.S. 307, 102 S.Ct. 3103, 73 L.Ed. 2d 787 (1982), and F.W. Woolworth Co. v. Taxation and Revenue Department of New Mexico, 458 U.S. 354, 102 S.Ct. 3128, 73 L.Ed. 2d 819 (1982), the business of the payors of the intangible income would also have to be found unitary with petitioner's business in order to be included in Wisconsin apportionable income in 1975.

The burden of proof is on the petitioner to show that the divisions, subsidiaries and dividend payors, mentioned above, are discrete business enterprises and are not part of petitioner's unitary business, W.R. Grace Company v. Wisconsin Department of Revenue, Wisconsin Tax Appeals Commission, Docket No. I–6459, issued February 12, 1985. The Commission determines that petitioner has failed to sustain its burden of showing that Realty, Sterling Park and the Investment Division were discrete business enterprises. The Commission determines that the petitioner has succeeded in meeting its burden as to the railroad subsidiaries, the foreign subsidiaries and the dividend payors in which petitioner held a minority interest. The Commission further determines that the income derived by petitioner from the operations of its Investment Division on short-term investments of its working capital was properly included by respondent in petitioner's 1975 Wisconsin apportionable income.

The term 'unitary business' has often been interpreted by state courts, and many of these state court decisions have been reviewed by the United States Supreme Court. While these cases are extremely helpful in establishing the general principles and matters of emphasis for the Commission to consider, they make it patently clear that the determination of whether a business is unitary in its operations rests on the facts of each case.

*12 In determining whether a unitary business exists, courts look to the 'underlying economic realities' of a multistate business, in that the 'form of business organization may have nothing to do with the underlying unity or diversity of business enterprise,' Mobil Oil Corporation v. Commissioner of Taxes, 445 U.S. 425, 100 S.Ct. 1223, 63 L.Ed. 2d 510, 523 (1980). There must be 'some sharing or exchange of value not capable of precise identification or measurement—beyond the mere flow of funds arising out of a passive investment or a distinct business operation—which

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renders formula apportionment a reasonable method of taxation,' Container Corporation of America v. Franchise Tax Board, ___ U.S. ___, 103 S.Ct. 2933, 77 L.Ed. 2d 545, 554 (1983). In such cases 'separate accounting, while it purports to isolate portions of income received in various states, may fail to account for contributions to income resulting from functional integration, centralization of management, and economies of scale,' Mobil, page 521.

Two recent cases, ASARCO, supra., and Woolworth, supra., 'seem to suggest something more is needed than evidence of common ownership, high-level executive oversight and certain centralized nonoperating functions such as accounting, legal and financing services, and something more than just adding to the profit of the parent; rather there must be some 'rational relationship' between the outside income attributed to the taxing state and the intrastate values of the enterprise so that the local in-state operation is more than simply a discrete business enterprise,' The Commissioner of Revenue v. Associated Dry Goods, Inc., 347 N.W. 2d 36 (Minn. 1984), citing ASARCO, 102 S.Ct. at 3114–15; and F.W. Woolworth, 102 S.Ct. at 3135. The Court, in holding that interest and dividend income received from foreign subsidiaries could not be included in taxable income in Idaho and New Mexico, held that the subsidiaries were 'discrete business enterprises, that—in 'any business or economic sense' have 'nothing to do with the activities' of ASARCO in Idaho,' ASARCO, p. 329.

The Court rejected two arguments made by the taxing states. First, the Court rejected the notion that an entity, merely by enhancing the resources and/or profit of a corporation, becomes part of a unitary business with the corporation. Secondly, the Court rejected the argument that 'mere potential to operate a company as a part of a unitary business' is sufficient to sustain a holding of unitariness, Woolworth, p. 362.

The Court in another recent decision, Container Corporation, supra., elaborated on the issue of 'potential control' holding, at p. 561, that

> In any event, although potential control is, as we have said in F.W. Woolworth, not 'dispositive' of the unitary business issue, it is relevant, both to whether or not the components of the purported unitary business share that degree of common ownership which is a prerequisite to a finding of unitariness, and also to whether there might exist a degree of implicit control sufficient to render the parent and the subsidiary an integrated enterprise.

*13 The Court in Container Corporation found two factors particularly noteworthy in its determination to uphold California's finding of unitariness between Container Corporation and foreign subsidiaries. First, the flow of capital resources by loans to its subsidiaries, clearly shows a flow of value. The Court stated that

> As we made clear in another context in Corn Products Co. v. Commissioner, 350 U.S. 50–53, 100 L.Ed. 29, 76 S.Ct. 20 (1955), capital transactions can serve either an investment function or an operational function. In this case appellant's loans and loan guarantees were clearly part of an effort to insure that the overseas operations of [appellant] continue to grow and to become a more substantial part of the company's strength and profitability. footnote 19, page 562.

Second, the Court recognized the managerial role played by Container Corporation in the operations of its subsidiaries. The Court stated as to this factor, in footnote 19, page 562, that

> We made clear in F.W. Woolworth, that a unitary business finding could not be based merely on 'the type of occasional oversight—with respect to capital structure, major debt, and dividends—that any parent gives to an investment in a subsidiary. . . . 458 U.S. at ——, 73 L.Ed. 2d 819, 102 S.Ct. 3128. As Exxon illustrates, however, mere decentralization of day-to-day management responsibility and accountability cannot defeat a unitary business finding. 447 U.S., at 224, 65 L.Ed. 2d 66, 100 S.Ct. 2109. The difference lies in whether the management role that the parent does play is grounded in its own operational strategy.

Against this background, we will first examine the facts relating to the Realty, Sterling Park and Investment Division. It is uncontroverted that these divisions, as with all of petitioner's divisions, operated with a high degree of autonomy and independence, under the principle of 'functional profitability independence.' Each division had responsibility for determining how best to achieve profitability.

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Each division (including the three at issue herein) had its own books and records and profit and loss statements. Each had its own sales, advertising, personnel, accounting, etc., departments. The divisions operated independently from one another, and intra-company sales and transactions were conducted on an arm's length basis.

Petitioner's central corporate office made many centralized services available to the divisions, e.g., assistance with personnel, purchasing, legal, tax, etc., matters. The divisions were not required to utilize these services and were charged a fee for doing so, which was taken against their profit and loss statements.

Although the divisions, including the three at issue, were relatively autonomous with respect to day-to-day operations, 'mere decentralization in day-to-day management responsibility and accountability cannot defeat a unitary business finding,' Container Corporation, supra., p. 562. The unitary business/formula apportionment principle may apply to vertically integrated enterprises or to 'a series of similar enterprises operating separately in various jurisdictions but linked by common managerial or operational resources that produced economies of scale and transfers of value,' Id., p. 554.

*14 Despite petitioner's decentralized management style, the elements of centralized management, functional integration and economies of scale were shown to exist in petitioner's operations.

Unity of ownership and centralized management have been shown. While it is true, as petitioner has argued, that all divisions within a single corporate shell need not be unitary, there exist certain inherent characteristics within a corporate shell which make a showing of 'discrete business' operations more difficult. The most obvious of these characteristics, which is present within petitioner corporation, is the existence of a single set of stockholders, a single Board of Directors and a single set of corporate officers. Although full unity of ownership alone may not be decisive, it is a factor, nevertheless, weighing heavily in favor of unitariness, see Comptroller v. Ramsay, Scarlett & Co., 473 A. 2d 469, 476 (Md. App. 1984).

Petitioner had an elaborate central management structure with divisions reporting to the central office at various levels by function, e.g., the top executives of Realty and Sterling Park reported to the Vice-President of Realty and Finance and the top executive of the Investment Division reported to the corporate Treasurer. Their hiring and firing was in the sole discretion of central management.

The ultimate control rested with the Board of Directors which delegated significant authority to the Corporate Policy and Corporate Management Committees. Divisional budgets, forecasts and facilities planning were centrally coordinated. Petitioner's central management provided the type of executive oversight that went beyond mere potential to some degree of implicit control, Container Corporation, p. 561.

There was functional integration. Petitioner's central office prepared tax returns for all divisions; prepared consolidated SEC reports; had a centralized computer system and a uniform accounting system; coordinated transportation needs; consolidated divisional budgets and facilities planning into a single company-wide plan; approved all divisional borrowing (whether from corporate funds or otherwise); and provided a wide range of technical assistance to divisions at their request, for a service charge. Employees were occasionally transferred inter-divisionally for training purposes. In addition to having a centralized coordination for steel and raw materials operations, petitioner had a Vice-President Accounting-Other Divisions whose responsibility was to work with the other divisions to make sure that petitioner had coordination and uniformity necessary to carry out its programs and policies.

All excess funds of the divisions flowed to the central office, were co-mingled with excess funds from other divisions, and were allocated at the discretion of top management for corporate expansion, capital improvements or acquisitions. This use of funds furthered the growth, strength and profitability of petitioner and showed the requisite 'flow of value,' Container Corporation, p. 562.

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*15 Economies of scale are present. Petitioner was a self-insurer on a company-wide basis; had a company-wide pension plan and employee insurance plans; and provided other centralized services which affected all divisions, e.g., lobbyists, company-wide advertising, personnel training programs, public relations and safety practices oversight. In addition, and perhaps most significantly, all divisional excess cash was co-mingled for short-term investment, thus obtaining a higher rate of return than if such funds remained separate.

While the record shows that petitioner has adopted a decentralized management style, the underlying economic reality of petitioner's operations has been one of substantial, active and implicit control over divisional operations which benefit from 'an umbrella of centralized management and controlled interaction,' Exxon Corp. v. Department of Revenue of Wisconsin, 447 U.S. 207, 65 L.Ed. 2d 66, 81, 100 S.Ct. 2109 (1980). There existed a 'flow of value' between the divisions and the central management, and petitioner's top management adopted a managerial role grounded in petitioner's own operational strategy, Container Corporation, p. 562. Therefore, the Commission has determined that the three divisions at issue were integral parts of petitioner's unitary business.

Petitioner has raised a second issue with regard to its Investment Division. Petitioner argues that under the holdings in ASARCO, supra., and Woolworth, supra., the payors of the intangible income derived from the operations of the Investment Division must be found to be unitary with petitioner's business in order to permit inclusion of this intangible income in Wisconsin apportionable income in 1975. The Commission has determined that this income was properly includable in Wisconsin apportionable income in 1975.

ASARCO and Woolworth did not deal with the type of intangible income derived from petitioner's Investment Division. In fact, ASARCO did not contend that income earned on short-term investments of its working capital was per se beyond the taxing power of a nondomiciliary state, and admitted that Idaho had the 'right to treat interest income from temporary deposits of [its] working capital funds as apportionable business income derived in the ordinary course of [its] Unitary Business activities.' See Justice O'Connor's Dissenting Opinion. Justice O'Connor points out that 'an appropriate amount of liquid working capital is necessary to the day-to-day operation of a business, and any return earned from its temporary investment is a byproduct of the operation of the business.'

Petitioner's Investment Division served this very function. The Division's main responsibility was to manage and invest petitioner's cash not needed for the day-to-day operations in short-term investments (most of which were negotiable and readily traded by the Division) and to provide needed cash flow, on short notice, for use by petitioner and its divisions.

Thus, the income derived from the operations of this Division was a by-product of petitioner's business and was, therefore, apportionable business income. The flow of cash in and out of this Division, for the liquid working capital necessary for petitioner's operations, is the single most unifying factor of petitioner's entire operation.

*16 Therefore, the Commission holds that the intangible income derived from short-term investment of petitioner's working capital was business income within the meaning of sec. 71.07(1m) and subject to apportionment, even though the underlying operations of the issuing entities were far less related to petitioner's unitary operations than the operations of petitioner's subsidiaries.

Petitioner has also met its burden of showing its twelve railroad subsidiaries to be 'discrete business enterprises.' Although as 100% owner of these companies, petitioner had the potential to control their operations, petitioner did not exert control over their operations.

The only evidence presented to show that there was unitariness was that there was a substantial amount of business conducted between the railroads and petitioner, and that petitioner made a single capital contribution to one of the companies in 1978 (after the audit period). The transactions between the railroads and petitioner were shown to be at

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arm's length and were subject to rigorous controls by the Interstate Commerce Commission.

Petitioner has also met its burden of proof in establishing that its foreign subsidiaries (Intupersa, Orinco Mining Company, Navios Corporation and Navigen Company) and its dividend payors in which petitioner owned a minority interest (Ashco, Inc., Oglebay Norton Co., Rinker Materials Co., Structural Dynamics and Altos Hornos) were discrete business enterprises. The Commission determines that the above-named corporations were not engaged in or a part of a unitary business with petitioner during the period at issue.

These corporations operated autonomously and independently from petitioner. These companies evidence neither functional integration, centralized management, nor economies of scale in conjunction with petitioner's operations. Theres was insufficient inter-dependence or inter-contribution to constitute a unitary business. Although petitioner's involvement with several of these companies evidenced one or more of the elements of unitariness, the requisite 'rational relationship', under ASARCO and Woolworth, between the dividend income paid by the companies attributed to Wisconsin and petitioner's unitary business in Wisconsin did not exist.

Petitioner contends that if intangible income is to be included in petitioner's 1975 apportionable income as business income, pursuant to the 1975 adoption of sec. 71.07(1m), Wis. Stats., set forth above, then all intangible proceeds from the sales, exchanges and redemptions of intangible assets, subject to apportionment, are to be included as 'total sales' for purposes of calculating the denominator of the sales factor. The Commission agrees with petitioner's contention.

In 1975, when sec. 71.07(1m) was enacted, the Wisconsin legislature did not change any portion of sec. 71.07(2), defining the apportionment factors. The relevant statutory section defines the denominator of the sales factor as 'total sales by taxpayer everywhere.' This broad definition remained the same and was not limited in any way by the legislature in 1975.

*17 At the time of the enactment of sec. 71.07(1m), respondent had further defined, under the provisions of Wis. Adm. Code sec. Tax 2.39(5)(a), the term 'sales' for purposes of the sales factor as 'generally all gross receipts derived by a taxpayer from transactions and activities in the course of its regular trade or business operations which produce business (apportionable) income.' Although respondent began the process of amending the Administrative Code section to limit the sales factor to only receipts from a taxpayer's 'principal' business activity, the amendment was never promulgated and sec. 2.39(5)(a) remained unchanged.

In September, 1977 (2 1/2 years after the enactment of sec. 71.07(1m)), respondent issued a Field Audit Section Bulletin 77–9, a non-public document, which directed respondent's field auditors to include only receipts from 'the main thrust of the taxpayer's business' (emphasis added) in calculating the numerator or the denominator of the sales factor.

Petitioner argues that because no statutory change to the factors was enacted and no change to the administrative rules was promulgated, there is no statutory authority for limiting the terms 'total sales' or 'all gross receipts derived . . . in the course of regular trade or business operations,' to only those receipts from the 'main thrust' of petitioner's business. Petitioner argues the 'total' means 'all', citing Transamerica Financial Corp. v. Wisconsin Department of Revenue, 56 Wis. 2d 57, 67, 201 N.W. 2d 522 (1972), which includes all proceeds.

Respondent argues that the term 'sales' when given its ordinary meaning, does not include dividend and other intangible income received by petitioner. Respondent further argues that petitioner is in the business of manufacturing and selling steel and related products and not in the business of investing, and that, therefore, the intangible income at issue was not derived from petitioner's 'regular trade or business operations.'

The Commission has determined, first, that petitioner's Investment Division, given the magnitude of its operation, was a part of its 'regular trade or business operations.' Even respondent's witnesses conceded that a corporation can have

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more than one line of regular business activity.

Further, the Commission determines that respondent's definition of 'total sales' as being limited to only receipts derived from the 'main thrust' of petitioner's business operations, is supported neither by statute nor by administrative rule. This definition is far more restrictive than provided for by statute.

Respondent's argument that the ordinary meaning of the word 'sales' does not encompass dividends and other intangible income ignores the definition provided in Wis. Adm. Code sec. 2.39(5)(a). Respondent also argues that based upon Wisconsin's adoption of UDITPA almost word for word, with the exception that Wisconsin did not adopt the UDITPA definition of 'sales' as 'all gross receipts of the taxpayer not allocated,' Wisconsin intended a more restrictive definition of sales than provided for in UDITPA. However, this argument ignores the fact that Wis. Adm. Code sec. 2.39(5)(a) is almost verbatim the UDITPA definition of 'sales', and sec. 2.39(5)(a) was in effect in 1975 and remains so.

*18 Therefore, the Commission determines that for 1975, under sec. 71.07(2), Wis. Stats., and Wis. Adm. Code sec. 2.39(5)(a) petitioner may properly include for purposes of calculating the sales factor of the apportionment formula, income from intangibles subject to apportionment in that year.

The Commission will only briefly comment on two additional issues raised by petitioner. Petitioner contends that the property, payroll and sales of petitioner's dividend paying subsidiaries should be included in the denominators of the property, payroll and sales factors for purposes of calculating intangible income apportionable to Wisconsin. The Commission has determined that such 'combined apportionment' is not provided for under Wisconsin law, Interstate Finance Corp. v. Department of Taxation, 28 Wis. 2d 262 (1965).

Second, petitioner having conceded that under the holding by the United States Supreme Court in Exxon, supra., Wisconsin has the authority to include in apportionable income petitioner's mining income, other than mining income derived from sales to third parties, contends that respondent's method of computing the amount of non-apportionable mining income derived from sales to third parties was arbitrary and/or in violation of the statutory pattern in sec. 71.07, Wis. Stats. The Commission has determined that petitioner has met its burden of showing respondent's method to be incorrect. Although there is no statute or regulation setting forth the proper method for making such a determination, the evidence shows that respondent's method is unreliable given the economic realities of mining operations and that petitioner's method, using the three factor approach, more accurately reflects petitioner's non-apportionable mining income.

Opinion Submitted by

Catherine M. Doyle, Commissioner

ATTACHMENT: 'NOTICE OF APPEAL INFORMATION'
WISCONSIN TAX APPEALS COMMISSION

NOTICE OF APPEAL INFORMATION

NOTICE OF RIGHTS FOR REHEARING OR JUDICIAL REVIEW, THE TIMES ALLOWED FOR EACH AND THE IDENTIFICATION OF THE PARTY TO BE NAMED AS RESPONDENT

The following notice is served on you as part of the Commission's decision rendered:

Any party has a right to petition for a rehearing of this decision within 20 days of the service of this decision, as provided in section 227.12 of the Wisconsin Statutes, a copy of which is printed on the reverse side hereto. The 20 day period commences the day after personal service or mailing of this decision. (Decisions of the Tax Appeals

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Commission are mailed the day they are dated. In the case of an oral decision, personal service is the oral pronouncement of the decision at the hearing.) The petition for rehearing should be filed with the Wisconsin Tax Appeals Commission. Nevertheless, an appeal can be taken directly to circuit court through a petition for judicial review. It is not necessary to petition for a rehearing.
Any party has a right to petition for a judicial review of this decision as provided in section 227.16 of the Wisconsin Statutes, a copy of which is printed on the reverse side hereto. The petition should be filed in circuit court and served upon the Wisconsin Tax Appeals Commission within 30 days of service of this decision if there has been no petition for rehearing, or within 30 days of service of the order finally disposing of the petition for rehearing, or within 30 days after the final disposition by operation of law of any petition for rehearing. The 30 day period commences the day after personal service or mailing of the decision or order, or the day after the final disposition by operation of law of any petition for rehearing. (Decisions of the Tax Appeals Commission are mailed the day they are dated. In the case of an oral decision, personal service is the oral pronouncement of the decision at the hearing.) The petition for judicial review should name the Department of Revenue as respondent and must be served upon that department within 30 days of filing the petition for judicial review in circuit court.

***19** This notice is part of the decision and incorporated therein.

Note: Section 227.12 and 227.16 Wis. Stats. see reverse side.

The statute sections shown in this material have been generated from the original data base of the 1981–82 Wisconsin Statutes, but may not be an exact duplication. Please refer to the 1981–82 Wisconsin Statutes for the official text.

227.12 Petitions for rehearing in contested cases. (1) A petition for rehearing shall not be a prerequisite for appeal or review. Any person aggrieved by a final order may, within 20 days after service of the order, file a written petition for rehearing which shall specify in detail the grounds for the relief sought and supporting authorities. An agency may order a rehearing on its own motion within 20 days after service of a final order. This subsection does not apply to s. 17.025(3)(e). No agency is required to conduct more than one rehearing based on a petition for rehearing filed under this subsection in any contested case.

(2) The filing of a petition for rehearing shall not suspend or delay the effective date of the order, and the order shall take effect on the date fixed by the agency and shall continue in effect unless the petition is granted or until the order is superseded, modified, or set aside as provided by law.

(3) Rehearing will be granted only on the basis of:

(a) Some material error of law.

(b) Some material error of fact.

(c) The discovery of new evidence sufficiently strong to reverse or modify the order, and which could not have been previously discovered by due diligence.

(4) Copies of petitions for rehearing shall be served on all parties of record. Parties may file replies to the petition.

(5) The agency may order a rehearing or enter an order with reference to the petition without a hearing, and shall dispose of the petition within 30 days after it is filed. If the agency does not enter an order disposing of the petition within the 30-day period, the petition shall be deemed to have been denied as of the expiration of the 30-day period.

(6) Upon granting a rehearing, the agency shall set the matter for further proceedings as soon as practicable. Pro-

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ceedings upon rehearing shall conform as nearly may be to the proceedings in an original hearing except as the agency may otherwise direct. If in the agency's judgment, after such rehearing it appears that the original decision, order or determination is in any respect unlawful or unreasonable, the agency may reverse, change, modify or suspend the same accordingly. Any decision, order or determination made after such rehearing reversing, changing, modifying or suspending the original determination shall have the same force and effect as an original decision, order or determination.

History: 1975 c. 94 s. 3; 1975 c. 414; 1977 c. 139; 1979 c. 208.

227.16 Parties and proceedings for review. (1) Except as otherwise specifically provided by law, any person aggrieved by a decision specified in s. 227.15 shall be entitled to judicial review thereof as provided in this chapter.

*20 (a) Proceedings for review shall be instituted by serving a petition therefor personally or by certified mail upon the agency or one of its officials, and filing the petition in the office of the clerk of the circuit court for the county where the judicial review proceedings are to be held. Unless a rehearing is requested under s. 227.12, petitions for review under this paragraph shall be served and filed within 30 days after the service of the decision of the agency upon all parties under s. 227.11. If a rehearing is requested under s. 227.12, any party desiring judicial review shall serve and file a petition for review within 30 days after service of the order finally disposing of the application for rehearing, or within 30 days after the final disposition by operation of law of any such application for rehearing. The 30-day period for serving and filing a petition under this paragraph commences on the day after personal service or mailing of the decision by the agency. If the petitioner is a resident, the proceedings shall be held in the circuit court for the county where the petitioner resides, except that if the petitioner is an agency, the proceedings shall be in the circuit court for the county where the respondent resides and except as provided in ss. 182.70(6) and 182.71(5)(g). The proceedings shall be in the circuit court for Dane county if the petitioner is a nonresident. If all parties stipulate and the court to which the parties desire to transfer the proceedings agrees, the proceedings may be held in the county designated by the parties. If 2 or more petitions for review of the same decision are filed in different counties, the circuit judge for the county in which a petition for review of the decision was first filed shall determine the venue for judicial review of the decision, and shall order transfer or consolidation where appropriate.

(b) The petition shall state the nature of the petitioner's interest, the facts showing that petitioner is a person aggrieved by the decision, and the grounds specified in s. 227.20 upon which petitioner contends that the decision should be reversed or modified. The petition may be amended, by leave of court, though the time for serving the same has expired. The petition shall be entitled in the name of the person serving it as petitioner and the name of the agency whose decision is sought to be reviewed as respondent, except that in petitions for review of decisions of the following agencies, the latter agency specified shall be the named respondent:

1. The tax appeals commission, the department of revenue.

2. The banking review board or the consumer credit review board, the commissioner of banking.

3. The credit union review board, the commissioner of credit unions.

4. The savings and loan review board, the commissioner of savings and loan, except if the petitioner is the commissioner of savings and loan, the prevailing parties before the savings and loan review board shall be the named respondents.

*21 (c) Copies of the petition shall be served, personally or by certified mail, or, when service is timely admitted in writing, by first class mail, not later than 30 days after the institution of the proceeding, upon all parties who appeared before the agency in the proceeding in which the order sought to be reviewed was made.

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(d) The agency (except in the case of the tax appeals commission and the banking review board, the consumer credit review board, the credit union review board, and the savings and loan review board) and all parties to the proceeding before it, shall have the right to participate in the proceedings for review. The court may permit other interested persons to intervene. Any person petitioning the court to intervene shall serve a copy of the petition on each party who appeared before the agency and any additional parties to the judicial review at least 5 days prior to the date set for hearing on the petition.

(2) Every person served with the petition for review as provided in this section and who desires to participate in the proceedings for review thereby instituted shall serve upon the petitioner, within 20 days after service of the petition upon such person, a notice of appearance clearly stating the person's position with reference to each material allegation in the petition and to the affirmance, vacation or modification of the order or decision under review. Such notice, other than by the named respondent, shall also be served on the named respondent and the attorney general, and shall be filed, together with proof of required service thereof, with the clerk of the reviewing court within 10 days after such service. Service of all subsequent papers or notices in such proceeding need be made only upon the petitioner and such other persons as have served and filed the notice as provided in this subsection or have been permitted to intervene in said proceeding, as parties thereto, by order of the reviewing court.

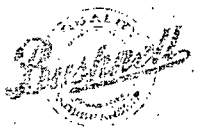
History: 1971 c. 243; 1975 c. 94 s. 3; 1975 c. 414; 1977 c. 26 s. 75; 1977 c. 187; 1979 c. 90, 208, 355.

The circuit court has no jurisdiction of an appeal from the tax appeals commission where the petition for review was served only on the department of revenue and not on the commission within the allowed 30 days. Brachtl v. Dept. of Revenue, 48 W (2d) 184, 179 NW (2d) 921.

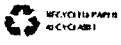
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Virginia State Tax Reporter, Ruling of Commissioner, P.D. 89-235-- Corporate Income-- Allocation and Apportionment-- Sales Factor-- Sales of Marketable Securities, Virginia, ¶201-815, (Sep. 6, 1989)

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¶201-815. Ruling of Commissioner, P.D. 89-235, , Virginia Department of Taxation, September 6, 1989.

Corporate Income: Allocation and Apportionment: Sales Factor: Sales of Marketable Securities.-- A manufacturer's gross proceeds derived from sales of marketable securities were properly included in the sales factor. The taxpayer had its commercial domicile in Virginia. In addition to income derived from manufacturing, the taxpayer earned a significant amount of income from investment and trading in securities. Insofar as the securities-related income involved selection, purchase and market-monitoring activites by employees whose salaries were included in the payroll factor, corporate income was not distorted when the gross receipts generated by the employees' activities were also included in the sales factor. Therefore, the use of an alternate method of allocation and apportionment was not justified.

This is in response to a conference held on October 17, 1988, in which you asked us to reconsider our ruling dated June 29, 1988, P.D. No. 88-172 (copy enclosed) [Not reproduced. CCH]. You also requested us to allow you to use an alternative method of allocation and apportionment.

FACTS

The taxpayer is a manufacturer with its commercial domicile in Virginia. In addition to its income from manufacturing, the taxpayer earns a significant amount of interest income from its investments in various forms of marketable securities and capital gain from trading in securities.

The inclusion of gross proceeds from these sales of securities in the numerator and denominator of the sales factor increased the sales factor from 7.6% to 37.0%. This adjustment accounts for most of the additional tax assessed.

DETERMINATION

You claim that the inclusion of the gross proceeds of security sales distorts the amount of income apportioned to Virginia. To illustrate this you point out that three alternative investments earning apportionable interest income have significantly different impacts on Virginia's sales factor:

- *Bank account:* The withdrawal of funds from a bank account is not a gross receipt for purposes of the sales factor.
- *Mutual fund:* The gross proceeds from the sale of mutual fund shares are included in the sales factor, but trading by the fund itself does not affect the taxpayer's sales factor.
- *Direct purchase of bonds:* The gross proceeds from the sale of the bonds are included in the sales factor.

It is recognized that each of the three types of investments has a different impact on the Virginia sales factor; however, that does not mean that the different tax treatment is unjustified. The direct purchase of a bond involves selecting, purchasing, and ongoing monitoring of the market interest rates and the issuer's credit rating. The salary and wages of the employees who engage in these activities are, of course, included in the payroll factor. There is no distortion when the gross receipts generated by an employee's activity are also included in the sales factor.

The selection and purchase of a mutual fund involves activities similar to the direct purchase of a bond, so gross proceeds from sales of mutual fund shares are appropriately included in the sales factor. The taxpayer's employees have no involvement in the trading activities of the mutual fund itself; thus the fund's sales do not affect the taxpayer's sales factor. Money deposited into a bank account is not a "purchase," nor is a withdrawal equivalent to a sale of property. Therefore, withdrawals from a bank account have never been included in the sales factor.

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Accordingly, the ruling dated June 29, 1988, P.D. No. 88-172, is reaffirmed. Since there is no distortion of income, there is not basis for finding that an alternative method of allocation and apportionment is justified. The assessment, as adjusted in accordance with the June 29, 1988 ruling, is correct.

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Virginia State Tax Reporter, Ruling of Commissioner, P.D. 87-77-- Corporate Income-- Allocation and Apportionment-- Sales Factor-- Proceeds from Sale of Stock, Virginia, ¶201-393, (Feb. 27, 1987)

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¶201-393. Ruling of Commissioner, P.D. 87-77, , February 27, 1987.

Corporate Income: Allocation and Apportionment: Sales Factor: Proceeds from Sale of Stock.-- Proceeds from the sale of stock were properly included in the numerator and denominator of the sales factor. The taxpayer purchased substantial amounts of stock a few days before dividends were paid and sold the stock a few days after dividends were paid. The proceeds came within the ordinary meaning of "gross receipts", and were not allocable dividends, but capital gains. The relevant income producing activity occurred in Virginia. There was no improper double taxation attributable to the apportionment method used by Virginia, and the taxpayer did not show that the standard method produced a clearly inequitable or unconstitutional result. Accordingly, the assessment was upheld. Secs. 58.1-414, 58.1-421, Code.

This is in response to your application dated September 20, 1985 for correction of an erroneous assessment of corporate income tax for the taxable year ended March 31, 1982.

FACTS

After a field audit the taxpayer was assessed additional tax. The taxpayer protests only the portion of the assessment attributable to the inclusion of certain proceeds from the sale of stock in the numerator and denominator of the sales factor.

In order to take advantage of the federal 85% special dividend deduction for dividends from domestic corporations, the taxpayer purchased substantial amounts of stock a few days before dividends were paid and sold the stock a few days after the dividends were paid. On the taxpayer's federal return the stock transactions were reported on Schedule D as short term gains and losses.

The auditor adjusted the sales factor to include the proceeds from the sales in the numerator and the denominator of the sales factor. The taxpayer protests the inclusion on the grounds that the proceeds were not gross receipts for purposes of the sales factor; that the receipts were derived from activity performed for the purpose of obtaining allocable dividends; that the income producing activity occurred in New York; and that the inclusion of the proceeds results in double taxation of income.

Gross Receipts

The sales factor includes all gross receipts of the corporation not allocated. Va. Code §§58.1-302, 58.1-414. Since the term "gross receipts" is not defined in the income tax chapter of the Virginia Code, the taxpayer refers to Va. Code §58.1-2600 where the term "gross receipts" is defined to exclude receipts from the sale of assets. The taxpayer contends that this definition should be applied to the sales factor to exclude proceeds from stock sales.

This definition is expressly limited by §58.1-2600 to use within the chapter on taxation of public service corporations and has no application to the income tax. In the absence of a statutory definition terms are given their ordinary meaning. The ordinary meaning of "gross receipts" would include all receipts or proceeds without reduction for expenses or basis. The fact the definition in §58.1-2600 expressly excludes receipts from the sale of assets is another indication that the ordinary meaning of the term "gross receipts" includes proceeds from the sale of stock. Therefore proceeds from the stock sales are gross receipts for the purpose of the sales factor.

Allocable Dividends

The taxpayer contends that the sole purpose of the transactions was to generate dividend income, which is allocable income under Virginia law. Because items which produce allocable income are excluded from the

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apportionment factors, the taxpayer claims that the proceeds from the stock sales should be excluded from the sales factor.

The ownership of stock may generate two types of income for federal and Virginia tax purposes: dividends and capital gain (or loss). The two types of income are defined under federal law and treated differently under federal law. It should be noted that the purpose of these transactions was to generate two types of income: dividends qualifying for the federal 85% special dividend deduction and fully deductible capital losses. Since Virginia begins with federal taxable income, Va. Code §58.1-402, and terms have the same meaning under both laws, Va. Code §58.1-301, the two types of income are recognized as different types of income under Virginia law. Allocable dividend income is limited to income treated as dividends under federal law. All other income, including capital gains and sale proceeds which generate capital gains, is included in apportionable income and the apportionment factors.

Income Producing Activity

The taxpayer appointed a New York agent to make all decisions about which stock to buy and sell for dividends. All purchases and sales were made in New York. The taxpayer contends that all income producing activity related to the stock sales took place in New York and that the proceeds should not be included in the numerator of the sales factor.

Not all of the income producing activity took place in New York. Some oversight and decision making occurred in Virginia where the headquarters and commercial domicile of the taxpayer is located. Virginia Regulation §630-3-416 states that the costs of indirect expenses, such as the activities performed by independent contractors and agents, is not included in determining the income producing activity associated with receipts. Therefore none of the costs of performance or income producing activity performed by the New York agent is taken into consideration in determining the location of receipts for the sales factor. The only other income producing activity associated with the receipts from these stock sales occurred at the commercial domicile of the taxpayer in Virginia. Therefore the receipts were properly included in the numerator.

Double Taxation

The taxpayer claims that it is subject to tax in twenty-nine states and that Virginia is the only one to include the receipts from stock sales in the sales factor. The inclusion significantly increases the Virginia sales apportionment factor and results in apportioning income to Virginia that other states also tax.

There is nothing unreasonable or unconstitutional about the method Virginia uses to allocate and apportion income. The taxpayer has not demonstrated that the income attributed to Virginia is out of all appropriate proportion to the business transacted in Virginia. Simply because two states have different methods of taxing income is no reason to find one of them unconstitutional. *Container Corp. of America v. Franchise Tax Board,* 463 U.S. 159 (1983), *Moorman Mfg. Co. v. Bair,* 437 U.S. 267 (1978).

Therefore the auditor properly included the receipts from the stock sales in the numerator and denominator of the sales factor and the assessment of additional tax was not erroneous.

Alternative Method

Your application also requested that an alternative method of allocation and apportionment be considered under §58.1-421. The requested method would exclude the receipts from both the numerator and denominator of the sales factor. Although the tax has not been paid, and thus the request does not comply with the procedures set forth in Va. Regulation §630-3-421, the request will be considered at this time.

In support of its request the taxpayer states that if the type of transactions involved had been carried out all year the sales factor would have been clearly distorted. The regulations of the Multistate Tax Commission and some other states contain authority for the exclusion of items from both the numerator and denominator of a factor if the items would distort the factor.

Virginia law contains detailed apportionment provisions. The only authorization for discretionary exclusion of items from the factors is in the alternative method provisions of §58.1-421. This section provides that the assessment may be reduced, but not increased, if it is found that the statutory method is inequitable.

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Thus the legislative intent is not to allow variations from the statutory method merely because the taxpayer believes that some other method may be more accurate. The department has previously stated that an alternative method is reserved for extraordinary situations where the taxpayer has shown by clear and cogent evidence that the statutory method produces an inequitable or unconstitutional result.

The inclusion of the stock sales causes the overall apportionment factor to increase by about five (5) percentage points. Even if one assumes, for the sake of argument, that inclusion of the stock sales distorts the measurement of income from Virginia sources, a difference of such a small amount does not justify such an extraordinary remedy as the allowance of an alternative method.

DETERMINATION

Accordingly, the assessment of additional tax is correct and is now due and payable. Permission to use an alternative method of allocation and apportionment is denied. You will shortly receive an updated bill with accrued interest to date. The bill should be paid within 30 days to avoid additional interest.

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2000 WL 1279835, 15 Or. Tax 202
(Cite as: 2000 WL 1279835 (Or.Tax Regular Div.), 15 Or. Tax 202)

Oregon Tax Court, Regular Division.
AT & T, for itself and on behalf of certain combined subsidiaries, Plaintiff,
v.
DEPARTMENT OF REVENUE, State of Oregon, Defendant.

No. 4438.
Aug. 31, 2000.

ORDER GRANTING PLAINTIFF'S MOTION FOR SUMMARY JUDGMENT

**203 BYERS, J.

*1 This appeal seeks to extend the holding of *Sherwin-Williams* [FN1] to a utility taxable under ORS 314.280.[FN2] Plaintiff (taxpayer) asserts that the statute and its accompanying administrative rules require gross receipts from invested working capital to be included in the sales-factor denominator. The matter is before the court on taxpayer's motion for summary judgment and Defendant Department of Revenue's (the department) response. The court has considered the memoranda submitted and oral arguments made July 20, 2000, in the courtroom of the Oregon Tax Court, Salem.

FN1. *Sherwin-Williams Co. v. Dept. Of Rev.*, 14 OTR 384 (1998), *aff'd* 329 Or 599, 996 P.2d 500 (2000).

FN2. All references to the Oregon Revised Statutes are to the 1987 replacement part.

FACTS

Taxpayer is a telecommunication company incorporated in New York. During the tax years in question, 1985 through 1989, taxpayer conducted business in Oregon as well as in other states. As a public utility within the meaning of ORS 314.610(6), taxpayer was required to report its Oregon taxable income in accordance with ORS 314.280. In doing so, taxpayer applied the three-factor formula prescribed by OAR 150-314.280-(A) through (F).

Taxpayer regularly invests working capital in short-term securities such as United States Treasury bills and bonds, commercial paper, certificates of deposit, and repurchase agreements. Its objective in making such investments is to earn income on otherwise idle cash. Taxpayer included the gross receipts from the sales and redemption of investment securities in the denominator of the sales factor used to compute its Oregon apportionment percentage.

The department audited taxpayer's returns and determined that only net income, not gross receipts, should be included in the denominator in the sales factor. The department recalculated the apportionment percentages, resulting in additional taxes owing for the years in question.

**204 ISSUE

Are gross receipts from the sales of intangibles by a public utility includible in the denominator of the sales factor?

ANALYSIS

In *Sherwin-Williams*, this court held that the definition of "sales" in ORS 314.610 as "gross receipts" necessarily included gross receipts from the sale of intangible assets. 14 OTR 384 (1998), *aff'd*, 329 Or 599, 966 P.2d 500 (2000). In that case, the taxpayer was a national corporation doing business interstate subject to taxation under ORS 314.605 to 314.675 (UDITPA). Here, taxpayer is a public utility taxable under ORS 314.280. That statute provides:

"(1) If a taxpayer has income from business activity * * * as a public utility * * * which is taxable both within and without this state * * * the determination of net income shall be based upon the business activity within the state, and the department shall have power to permit or require either the segregated method of reporting or

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the apportionment method of reporting, under rules and regulations adopted by the department, so as fairly and accurately to reflect the net income of the business done within the state."

Taxpayer elected to use the apportionment method. The department does not dispute taxpayer's use of that method but contends that taxpayer cannot include gross receipts from the sale of intangibles. Taxpayer points to the "rules and regulations adopted by the department" as authorized by ORS 314.280. One of those rules, OAR 150-314.280-(B), states:

*2 "The definitions of 'business income,' 'commercial domicile,' 'compensation,' 'financial organization,' 'non-business income,' 'public utility,' 'sales,' and 'state,' contained in ORS 314.610 and the related rules are by this reference incorporated herein and made a part of this OAR 150-314.280-(B).

" 'Taxpayer' means a financial organization or a public utility."

Taxpayer reasonably argues that if the state directs taxpayer to use the same method and definitions that were **205 construed and applied by the Supreme Court in *Sherwin-Williams*, it will arrive at the same result.

The department's response is less than crystal clear. The department acknowledges that it "did have and continues to have rules that incorporate by reference ORS 314.610" for the definition of sales. (Def's resp. at 10.) However, the department argues that there is no presumption of correctness as there is under UDITPA. The department asserts that "if a correction to a factor, as reported by the taxpayer, more fairly and accurately apportions net income, then the defendant must make such correction." *Id.* The department cites as authority for that position OAR 150-314.280-(M) as amended December 28, 1995. (Def's resp. Ex D at 1.)

This court must look to the law in effect during the years in question. During the period 1985 through 1989, ORS 314.280 gave the department limited power. It could require the taxpayer to use either the segregated method or the apportionment method of reporting. However, that power was to be exercised "under rules and regulations" that insured whichever method was required would "fairly and accurately" reflect the net income of the business done within the state. The rule in effect during the years in question, OAR 150-314.280-(M), stated:

"If the allocation and the apportionment provisions of OAR 150-314.280-(A) to 150-314.280-(L) do not fairly represent the extent of the taxpayer's business activity in this state *and* result in the violation of the taxpayer's rights under the Constitution of this state or of the United States, the taxpayer may petition for and the department may permit, or the department may require, in respect to all or any part of the taxpayer's business activity:

"(1) Separate accounting;

"(2) The exclusion of any one or more of the factors;

"(3) The inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or

"(4) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income." (Emphasis added.)

**206 The scope of the rule is clearly limited to situations where the apportionment provisions do not fairly represent the extent of the taxpayer's business activity in the state *and* results in a violation of the taxpayer's constitutional rights. There is no claim here that taxpayer's rights were violated under the constitution. Therefore OAR 150-314.280-(M) is not applicable.

*3 As noted, the department amended OAR

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150-314.280-(M) effective December 31, 1995, eliminating the requirement of a constitutional violation. However, it continues to allow only a change in the method of apportionment, such as excluding a factor or including additional factors. The rule does not and has never indicated that the department can unilaterally redefine "sales" or "gross receipts" on an ad hoc basis to suit its concept of fairness.

The department contends that as a result of the Supreme Court's decision in *Fisher Broadcasting, Inc. v. Dept. of Rev.*, 321 Or 341, 898 P.2d 1333 (1995), there is a "rebuttable presumption" in favor of the department's "sales factor." *Fisher* held that the legislature did not intend for public utilities taxable under ORS 314.280 to be subject to the presumptive-apportionment rules of UDITPA. The Supreme Court found that the focus of ORS 314.280 is on fair and accurate reporting of net income. As the department itself points out, *Fisher* held that utility taxpayers were left under the pre-existing regulatory regime of ORS 314.280. 321 Or at 354. The key words are "regulatory regime." The department is not trying to enforce its regulatory regime but is acting contrary to it. The department is not proposing a new or different method of reporting, but a new definition of sales. The department cannot "correct" its own definition of sales in that manner, otherwise the rules become meaningless.

The department argues that inclusion of gross receipts from sales of securities and other intangibles clearly distorts taxpayer's apportionable income. That may be, but the remedy is not an ad hoc "rewriting" of its own rules. As in *Sherwin-Williams*, the resolution must be by amendment of the statute or administrative rule.

**207 The department also argues that OAR 150-314.665-(3)(2) prohibits inclusion of gross receipts. However, that rule applies only if the business income from intangible property "cannot readily be attributed to any particular income producing activity of the taxpayer." OAR 150-314.665-(3)(2) defines income-producing activity as "transactions and activity directly engaged in by the taxpayer in the regular course of its trade or business for the ultimate purpose of obtaining gains or profit." The rule indicates that such activity includes but it is not limited to "the sale, licensing, or other use of intangible personal property." *Id.* Actively investing and reinvesting in securities is a particular income-producing activity engaged in for the ultimate purpose of obtaining gains or profit. Because the income is attributed to a particular income-producing activity, it does not come within the ambit of the above rule.

The department suggests that taxpayer's gross receipts from its investments do not constitute gross receipts as that term is used in the statute. OAR 150-314.280-(B) adopts the definition of "sales" as found in ORS 314.610 and the related rules. ORS 314.610 defines sales as "all gross receipts" not allocated under ORS 314.615 to 315.645. Neither the statutes nor the department's rules define gross receipts. The primary focus of OAR 150-314.610 is in distinguishing business income from nonbusiness income. That rule applies a broad definition of business income intended to cover almost any profit-oriented activity. There is no question that taxpayer's income from its investment activity is business income.

*4 The department argues that including gross receipts from investing of intangibles distorts the sales numerator because much of it is a return of capital. However, that is true of many sales, particularly of tangible property. In fact, the department's rules take a broad approach and apparently intend to cover situations where many of those receipts constitute a return of capital. Taxpayer's affidavits indicate that taxpayer regularly invests its working capital in securities to obtain income and profit from the purchase, sale, and redemption of securities. There are no contrary facts or affidavits to indicate that those amounts do not constitute gross receipts.

**208 Based on the above analysis, the court concludes that the department's rules by definition

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require the inclusion of gross receipts from the sale of intangibles in the sales denominator. Now, therefore,

IT IS ORDERED that Plaintiff's Motion for Summary Judgment is granted. Plaintiff to recover costs.

Or.Tax Regular Div.,2000.
AT&T v. Department of Revenue
2000 WL 1279835, 15 Or. Tax 202

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2000 WL 1025573, 15 Or. Tax 101
(Cite as: 2000 WL 1025573 (Or.Tax Regular Div.), 15 Or. Tax 101)

Oregon Tax Court, Regular Division.
PENNZOIL COMPANY and Subsidiaries, Plaintiff,
v.
DEPARTMENT OF REVENUE, State of Oregon, Defendant.

No. 4301.
March 17, 2000.

OPINION

**102 BYERS, J.

*1 Pennzoil and its subsidiary corporations (collectively referred to as Pennzoil) appeal from an assessment of additional corporate excise taxes for the 1988 tax year. That assessment arose out of a very large tort settlement received by Pennzoil. Defendant Department of Revenue (the department) contends that the settlement proceeds constitute apportionable unitary business income. The parties stipulated to some facts, and a trial was held to receive evidence with regard to others.

FACTS

Although Pennzoil is a century-old Pennsylvania oil company name, it is a Delaware corporation with its principal place of business in Texas. During the years in question, Pennzoil constituted a vertically integrated business that explored for, produced, refined, packaged, and sold oil. It also engaged in business activities related to oil, natural gas, and minerals. Its only business activities in Oregon were the distribution and sale of motor oil and related automotive products, and the activities of a small subsidiary. The Oregon subsidiary provided management information services to other Pennzoil operating subsidiaries and sold computer software.

In 1983, Pennzoil's chief executive officer saw an opportunity: Getty Oil Company (Getty Oil), with assets estimated in excess of $10 billion, was experiencing conflict among its major shareholders. Apparently, testamentary **103 conditions imposed by the late J. Paul Getty were the source of internal discord, resulting in stock values that were far less than asset values. After receiving authorization from Pennzoil's board of directors, on December 28, 1983, Pennzoil made a "friendly" tender offer for 20 percent of the Getty Oil stock. Within days, Pennzoil and Getty Oil reached an understanding and began preparations to formalize their agreement. That understanding contemplated a merger of the two companies and a restructuring of Getty Oil.

Unbeknownst to Pennzoil, Texaco Inc. (Texaco), another large oil company, began secretly negotiating with Getty Oil to buy all of its stock. By January 6, 1984, Texaco had a new agreement with Getty Oil and the two companies merged on February 17, 1984. Upon learning of the Texaco-Getty Oil agreement, Pennzoil sued Getty Oil for specific performance. When a Delaware court denied Pennzoil that equitable remedy, Pennzoil sued Texaco in Texas for improper interference with a contract. The jury trial awarded Pennzoil a judgment for $11,120,976,110.83 in damages.[FN1] After Texaco's appeals were denied, it filed bankruptcy. This prompted negotiations between Pennzoil and Texaco, resulting in a settlement agreement. On April 7, 1988, Texaco paid Pennzoil $3 billion in satisfaction of Pennzoil's claims in accord with the settlement agreement.[FN2] When Pennzoil filed its 1988 Oregon consolidated excise tax return (amended), it treated the net settlement proceeds as nonbusiness, nonapportionable income.[FN3] The department disagreed with this characterization and assessed additional corporate excise taxes. Pennzoil then commenced this appeal.

FN1. District Court of Harris County, Texas, judgment entered December 10, 1985. *See* Stipulation of Facts, Exhibit M.

FN2. As of March 31, 1988, in a move apparently intended to avoid state taxation of the settlement proceeds, Pennzoil Company conveyed all of its oil and gas assets to a new subsidiary, thereby converting itself into a holding company. The court considers that action and Pennzoil's holding company status irrelevant to the issues raised by the pleadings.

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FN3. The parties have stipulated that the amount in dispute is $2,088,840,687. (Stipulation of Facts at 1.)

**104 ISSUES

*2 Are the tort settlement proceeds unitary business income apportionable to Oregon? If so, should the gross proceeds from financial instruments in which the $3 billion was invested be included in the denominator of the sales factor?

ANALYSIS

Corporations doing business in Oregon are subject to an excise tax, measured by taxable income. ORS 317.070.[FN4] Pennzoil Company functioned as an operating company and was the reporting parent in the Oregon combined group. Because Pennzoil engages in business in more than one state, federal constitutional limitations on the state's jurisdiction to tax require its income to be apportioned.

FN4. All references to the Oregon Revised Statutes are to the 1987 Replacement Part.

To promote uniform taxation of interstate businesses, Oregon and a number of other states have adopted the Uniform Division of Income for Tax Purposes Act (UDITPA). *See* ORS 314.605 to 314.670. That statutory scheme provides the familiar three-factor formula for apportioning business income.[FN5] Nonbusiness income is not apportioned by a formula but is allocated based upon the source of the income. The critical question here is whether the tort settlement proceeds constitute business income.

FN5. ORS 314.650(1) provides in part that:

> " * * * All business income shall be apportioned to this state by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is three."

ORS 314.610(1) states in part:

" * * * 'Business income' means income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, the management, use or rental, and the disposition of the property constitute integral parts of the taxpayer's regular trade or business operations."

**105 ORS 314.610(5) states:

" 'Nonbusiness income' means all income other than business income."

In construing a statute, the court's first duty is to ascertain the intent of the legislature. Normally, this is done by first looking to the text and context of the statute. *PGE v. Bureau of Labor and Industries*, 317 Or 606, 859 P.2d 1143 (1993). However, UDITPA was adopted with the intent to achieve uniformity in the taxation of interstate businesses. Accordingly, the legislature directs that:

> "(2) ORS 314.610 to 314.670 shall be so construed as to effectuate its general purpose to make uniform the law of those states which enact it." ORS 314.605.

On its face, that statute suggests that the decisions of other states construing UDITPA should be considered by this court.

The Oregon Supreme Court has indicated that the two basic goals of UDITPA are: "(1) fair apportionment of income among the taxing jurisdictions; and (2) uniformity of the application of the statutes ." *See Twentieth Century-Fox Film v. Dept. of Rev.*, 299 Or 220, 227, 700 P.2d 1035 (1985). Thus, the Oregon Supreme Court has concluded that the legislature intended fairness and uniformity to be the guiding standards.

Oregon is also a member of the Multistate Tax Compact (MTC), a cooperative effort between some states to reduce administrative costs of auditing interstate businesses and to increase uniformity of interstate taxation. *See* ORS 305.655 through 305.685. The MTC has recommended a rule defining business income that Oregon has adopted as OAR 150-314.610(1)-(B). That rule provides in relevant part:

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*3 " * * * The classification of income by the labels occasionally used, such as manufacturing income, compensation for services, sales income, interest, dividends, rents, royalties, capital gains, operating income, nonoperating income, etc., is of no aid in determining whether income is business or nonbusiness income. Income of any type or class and from any source is business income if it arises from transactions and activity occurring in the regular course of a trade or **106 business. Accordingly, the critical element in determining whether income is 'business income' or 'nonbusiness income' is the identification of the transactions and activity which are the elements of a particular trade or business. In general, *all transactions and activities of the taxpayer which are dependent upon or contribute to the operations of the taxpayer's economic enterprise as a whole constitute the taxpayer's trade or business* and will be transactions and activity arising in the regular course of, and will constitute integral parts of, a trade or business. * * * " (Emphasis added.)

The validity of this rule was challenged in *Atlantic Richfield Co. v. Dept. of Rev.*, 300 Or 637, 645, 717 P.2d 613 (1986). In that case, the Oregon Supreme Court held that the rule would be upheld if: "(1) the application of the formula by the department reasonably approximates the taxpayer's income in Oregon, and (2) the application of the rule by the department 'effectuates [the] general purpose to make uniform the law of those states which enact [UDITPA] .' " *Id.* At 645. This broadly worded rule suggests that "fairness" is grounded in the elements of the business and how those elements relate to each other. If the elements are interrelated as part of an integrated or unitary business, the rule would tax all income produced by that business.

Oregon's power to tax is limited by the due process and commerce clauses of the United States Constitution. When imposing an income-based tax on an interstate business, a state may not tax value earned outside its border. *ASARCO Inc. v. Idaho State Tax Comm'n*, 458 U.S. 307, 315, 102 S Ct 3103, 73 L.Ed.2d 787 (1982). However, where a single integrated business operates in more than one state, its entire net income may be fairly apportioned among the states in which it operates. *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 79 S Ct 357, 3 L.Ed.2d 421 (1959).

" * * * [T]he linchpin of apportionability in the field of state income taxation is the unitary-business principle." *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 439, 100 S Ct 1223, 63 L.Ed.2d 510 (1980).

The unitary business principle provides the "minimal connection" needed to satisfy both due process and the **107 commerce clause. It is the "rational relationship between income attributable to the state and the interstate values of the enterprise." *Exxon Corp. v. Wisconsin Dept. of Rev.*, 447 U.S. 207, 219-20, 100 S Ct 2109, 65 L.Ed.2d 66 (1980). In commenting on this necessary relationship, the U.S. Supreme Court in *Container Corp. v. Franchise Tax Bd.*, 463 U.S. 159, 166, 103 S Ct 2933, 77 L.Ed.2d 545 (1983) stated in part:

*4 " * * * [T]he principles we have quoted require that the out-of-state activities of the purported 'unitary business' be related in some concrete way to the instate activities. The functional meaning of this requirement is that there be some sharing or exchange of value not capable of precise identification or measurement-beyond the mere flow of funds arising out of a passive investment or a distinct business operation-which renders formula apportionment a reasonable method of taxation."

In that same case the court noted that UDITPA's definitions of business income and nonbusiness income "track in large part the principles we have just discussed." *Id.* at 167. It therefore appears that the fairness required by the United States Constitution is found in the elements of the business, i.e., a unitary relationship. It also appears that applying constitutional standards would achieve some measure of uniformity because every state must comply with the requirements of the United States Constitution.

In light of all of the above, the court concludes that the Oregon legislature intended to tax interstate businesses to the extent allowed by due process and the

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commerce clause. The legislature has evidenced this intent in regard to other provisions of UDITPA. *See Maytag Corp. v. Dept. of Rev.*, 12 OTR 502 (1993).

This conclusion impacts the court's construction of ORS 314.610(1). Specifically, ORS 314.610(1) has two separate clauses that most jurisdictions view as imposing two separate tests. The first clause adopts a transactional test, i.e., whether income arises from transactions and activities in the regular course of the trade or business. The second clause incorporates a functional test, i.e., income from property is business income if the acquisition, management, use, or rental and disposition of the property constitute an integral **108 part of the regular trade or business. As indicated, some jurisdictions apply only the transactional test, whereas other jurisdictions apply both tests. *See* I Jerome R. Hellerstein & Walter Hellerstein, *State Taxation*, ¶ 9.05[2] at 9-33 (3rd ed 1998).[FN6]

> FN6. The authors acknowledge the functional test but do not believe it can be justified based on the language. They state: "[i]n short, despite the compelling policy reasons for adoption of the functional test, we do not believe that the language of UDITPA authorizes it." *Id.* at 9-45.

Although no Oregon court expressly so holds, ORS 314.610(1) has been construed as incorporating both the transactional and functional test. *See Simpson Timber Company v. Dept. of Rev.*, 13 OTR 315 (1995), aff'd. 326 Or 370, 953 P.2d 366 (1998). This court believes the legislature recognized the compelling policy reasons for the functional test and intended it to be used when it adopted ORS 314.610(1).

In applying the transactional test, the first question is: from whence did the income arise? Pennzoil contends that the tort lawsuit was the transaction or activity giving rise to the income. However, Pennzoil ignores a clearly established principle that is found in both federal and state income tax laws. That principle is: amounts received in litigation have the same character for income tax purposes as if collected without the necessity of lawsuit. *Hort v. Commissioner*, 313 U.S. 28, 61 S Ct 303, 85 L Ed 1168 (1941). Certainly a lawsuit to collect money owing on an open account for purchases of goods does not convert the income collected to something other than proceeds from the sale of goods. Likewise, damages received as compensation for loss of profits due to a tort or breach of contract are taxable as ordinary income. *Mertens Law of Federal Income Taxation* § 24A:23.

*5 UDITPA is merely an accounting method for taxing the income of interstate businesses. It does not extend the state's jurisdiction to tax, provide a new form of tax, or change the character of income for taxation purposes. Therefore, it should not be construed to change the character or source of income.

> " * * * In determining how damages recovered through litigation or settlement are treated for federal income tax purposes, courts have generally resolved that issue by asking: **109 'In lieu of what were the damages awarded?'" Hellerstein at ¶ 9.13[2][a].

That was the principle applied in *Simpson Timber Company v. Dept. of Rev.*, 13 OTR 315 (1995), aff'd. 326 Or 370, 953 P.2d 366 (1998) and in *Polaroid Corp. v. Offerman*, 349 N C 290, 507 S.E.2d 284 (1998), cert. denied, 119 S Ct 1576 (1999).

The preponderance of the evidence in this case establishes that the income arose from Pennzoil's agreement with Getty Oil Company (Getty contract). The existence of the Getty contract gave Pennzoil a right to damages for its breach and a right to damages for improper interference. Except for that contract, there would be no recovery and no income.

Initially, Pennzoil sued Getty Oil for specific performance. Failing to obtain that, Pennzoil then sued Texaco for interference of contract. In the Texaco suit, Pennzoil claimed damages for loss of bargain on the Getty contract based on the amount that Pennzoil would have saved in finding and developing 1 billion barrels of oil reserves. (Def's Ex FF at 48-49.) It is the same as if Pennzoil said to Texaco: you stole our deal, pay us what we would have benefitted. (TR at 60.) In the court's view, it does not matter whether the contract was sold, stolen, condemned, interfered with, or canceled;

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the income realized from it by Pennzoil was income "arising from" that contract.

The next question under the transactional test is whether negotiation of the contract with Getty Oil Company was an activity or transaction in the regular course of Pennzoil's trade or business. To answer this question, the court must consider what constitutes Pennzoil's regular trade or business.

Pennzoil offered no specific evidence as to how often or what kinds of agreements it negotiates for the sale or acquisition of oil and gas assets. However, some of the evidence touches upon the nature of Pennzoil's business. Pennzoil's offer to purchase the Getty stock stated:

> " * * * Pennzoil is a natural resource company engaged in oil and gas exploration and production, in processing, refining and marketing of oil and gas and refined petroleum products and in mining and processing of copper, molybdenum, silver, gold, sulfur and potash." (Stipulation of Facts, E at 8.)

**110 Pennzoil's explanation of how it proposed to pay for the Getty Oil stock indicates that most of the funds were to come from a production payment representing the sale of interests in numerous oil and gas leaseholds and fee interests. (Stipulation of Facts, E at 9-10.) Also, various activities mentioned in Pennzoil's annual reports (Def's Ex AAA-GGG) are consistent with the activities of a large oil and gas company that regularly engages in transactions and activities to acquire, use, or dispose of oil and gas assets. For example, in its 1984 annual report, the year the Getty contract was entered into, Pennzoil reports that it "participated in a number of major oil and gas plays, both domestically and internationally." (Def's Ex BBB at 8.)

*6 Pennzoil obviously follows the industry practice of acquiring participating interests in various projects or assets and forming partnerships for acquisitions and operations of oil and gas assets. (Def's Ex BBB at 36.) All of these descriptions suggest that acquiring interests in oil and gas properties or in properties having potential for oil and gas is one of the elements of Pennzoil's regular trade or business.

Texaco argues that the contract was to acquire stock, not oil and gas assets. However, it is clear that the plan was to add the Getty Oil reserves to Pennzoil's inventory. (Def's Ex JJJ at 8.) Buying the Getty Oil stock was just a less expensive way of obtaining reserves (Def's Ex KKK at 138). In the Texaco trial, Hugh J. Liedtke, the chief executive officer of Pennzoil and principal negotiator, testified:

> "Now, if * * * if we felt that we would have to own the stock forever, no, we wouldn't pay that for it. But we had, in our agreement, the ability to get assets and that's really what we're after. Principally oil and gas assets." (Def's Ex KKK at 144.)

When asked if the intent was to own the stock, or was it a way to purchase assets, he answered "[w]ell, the answer is we were after assets only. You had to buy some stock first to get there." (Def's Ex KKK at 144.)

Although the Getty contract was large, perhaps the largest ever negotiated by Pennzoil and certainly the richest, the preponderance of the evidence indicates that the transaction was in the course of its regular trade or business. The creation of that valuable asset by the efforts of Pennzoil's officers and employees through negotiation is no different than **111 the discovery of a new oil field by its engineers or a new method of marketing by its sales staff. Pennzoil regularly acquires, develops, and uses oil and gas assets and that is precisely why it entered into the Getty contract. The court finds that negotiating the Getty contract was an activity in the regular course of Pennzoil's unitary business. Any income arising from that transaction or activity is business income apportionable under UDITPA.

Under the functional test, the question is: does the acquisition, management, use or rental, and disposition of intangible property such as the Getty contract constitute an integral part of Pennzoil's regular trade or business? As indicated above, the preponderance of the evidence demonstrates that Pennzoil regularly acquires, uses, and disposes of contracts, stock, partnership interests, leases, and other interests in oil and gas assets.

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In the Texaco trial, the chief executive officer testified that he negotiated such purchases and sales many times over the years. (Def's Ex MMM at 32.) The officers of Pennzoil spent many years trying to "grow" the company (Def's Ex KKK at 85) and had previously had joint operations with Getty Oil Company. (Def's Ex KKK at 104.)

As one example, in 1983, Pennzoil, with a group of other "institutional and other investors," formed Proven Properties, Inc. for the purpose of acquiring and operating oil and gas producing properties. (Def's Ex EE at 8.) During 1984, Proven Properties, Inc. purchased interest in three Gulf of Mexico offshore oil leases and "various interests" in onshore gas producing properties. (Def's Ex EE at 8.) In the trial in this court, Baine P. Kerr, president of Pennzoil when the Getty contract was negotiated, testified that Pennzoil might have been able to form a joint venture or partnership with Getty. (TR at 46.) He also indicated that reserves are very important to Pennzoil (TR at 52) and that Pennzoil has leases for oil and gas numbering in the thousands. (TR at 51.)

***7** It is clear that before, during, and after 1984, Pennzoil was actively engaged in acquiring and disposing of interests in oil and gas assets as an integral part of its regular trade or business. It is also clear that the form of those acquisitions, whether stock, partnership interests, or otherwise, is immaterial. The court finds that the Getty contract was intangible property whose acquisition, use, and disposition constituted an integral part of the Pennzoil's regular ****112** trade or business. Except for the size and richness of the prize, it was no different than any number of other transactions over the years.

Applying the functional test, did the income come "from" that intangible property? Again, Pennzoil contends that the settlement income came from a lawsuit for tortious interference with contract and not from the contract itself. The court acknowledges that a claim for improper interference of contract is different from a claim for breach of contract. The two claims involve different parties, different tests for recovery, and to some extent, different measures of damages. However, the issue is not whether they are different claims. The issue is the source or origin of income. If the income arose from the Getty contract, any actions Pennzoil may have had to take in order to collect that income is irrelevant to its character or nature for income tax purposes.

Despite Pennzoil's arguments to the contrary, the court finds that *Simpson Timber* and *Polaroid* are very relevant. In *Simpson Timber*, the government took the taxpayer's property by power of eminent domain. 13 OTR 315 (1995), aff'd. 326 Or 370, 953 P.2d 366 (1998). In *Polaroid*, Kodak infringed Polaroid's patent rights. 349 N C 290, 507 S.E.2d 284 (1998). In both cases, property of the taxpayer was taken or appropriated by another party and damages paid in lieu of that property. Those damages were business income. Here, Texaco misappropriated Pennzoil's property. The settlement between Texaco and Pennzoil was in satisfaction of all claims by Pennzoil including its suit for specific performance of its contract.

Pennzoil argues that it only held the Getty contract three days and therefore it could not have been an integral part of its business. (Ptf's Post-Trial Brief at 38.) However, ORS 314.610(1) contains no time limits. What is particularly important about the Getty contract is that it was not property acquired from outside the business like an oil derrick or piece of refinery equipment that had to be integrated into the unitary operation. Its very creation was a result of Pennzoil's unitary business activities. Consequently, it was inherently an integral part of Pennzoil's regular trade or business.

****113** Pennzoil contends that taxation of the settlement proceeds violates the United States Constitution on two separate grounds. First, it contends Oregon has no nexus or minimal connection with the settlement proceeds, therefore it is taxing value earned outside of Oregon. This argument erroneously assumes that the income is not from the Getty contract. Because the income does arise from the Getty contract and that contract was part of Pennzoil's regular trade or business, the unitary business provides the required nexus with Oregon. Pennzoil's oil wells in Louisiana and offshore of California are economically integrated with the packaging and selling of oil in Oregon. Any gains or losses suffered by one part of the unitary business are suffered

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by the whole.

*8 Pennzoil assumes that its operations in Oregon had no connection with negotiating the Getty contact in New York. Nothing could be further from the truth. Regardless of the negotiating skills of Pennzoil's officers and employees, a contract with Getty Oil was possible only because of Pennzoil's unitary business. Without that business, Pennzoil's negotiators had nothing to offer and nothing to bring to the proposed merger table. It is the very "sharing or exchange of value not capable of precise identification or measurement" that makes Pennzoil's interest in the contract a unitary interest. *Container Corp.* at 166. Consequently, no one part of the integrated business and no one location can be identified as nonessential in the negotiating activity that gave rise to the Getty contract. The values, expectations, synergies, markets, and other characteristics of the Oregon operations were mingled with and as involved as any other part of the Pennzoil business.

Pennzoil cites *Allied-Signal v. Director, Tax Div.*, 504 U.S. 768, 112 S Ct 2251, 119 L.Ed.2d 533 (1992) as authority for arguing that no unitary relationship exists between Getty Oil and Pennzoil.[FN7] Again, Pennzoil is looking **114 beyond the mark. The Getty stock was not acquired, therefore no income arose from that stock. The only thing acquired were contract rights and contract obligations under the Getty contract. Therefore, the Getty contract must be the source of income. The only question under *Allied Signal* is whether the Getty contract served an operational function or an investment function.

> FN7. There is no doubt that if Pennzoil had acquired the Getty stock, there would be a unitary relationship.

> " * * * When a corporation invests in a subsidiary that engages in the same line of work as itself, it becomes much more likely that one function of the investment is to make better use-either through economies of scale or through operational integration or sharing of expertise-of the parent's existing business-related resources." *Container Corp. v. Franchise Tax Bd.*, 463 U.S. 159, 178, 103 S Ct 2933, 77 L.Ed.2d 545 (1983).

> " * * * That is the relevant unitary business inquiry, one which focuses on the objective characteristics of the asset's use and its relation to the taxpayer and its activities within the taxing State." *Id.* at 785.

Because the Getty contract was created by and arose out of Pennzoil's unitary business, there is no doubt that it served an operational function.

Pennzoil's second constitutional argument is that inclusion of the settlement income results in such distortion that Oregon is effectively taxing value earned outside the state. Pennzoil asserts that the income is out of all proportion to activities that take place in the state. Of course, this argument would apply equally to *every* state in which Pennzoil conducts its business. The $3 billion settlement was such a large amount it would cause distortion in every state based on the "normal" business activities in that state. In essence, Pennzoil believes that the settlement was too big to be taxed.

Pennzoil's energetic arguments are driven primarily by the amount involved. There is no doubt that if Pennzoil had sold the Getty contract to Texaco for three hundred thousand dollars or even $3 million, it would have been treated as business income without hesitation. The fact that the amount was $3 billion suddenly makes any taxation seem wrong to Pennzoil. However, just because a unitary business suddenly realizes more income than normal does not make it nonunitary. The court can find no basis for separating transactions based on size alone.

*9 Pennzoil's separate accounting purports to show that its operations in Oregon suffered a $1 million loss. Therefore, Pennzoil argues it is entirely wrong to attribute a $11.3 million income to such operations. In trying to gain some perspective on this argument, the court has looked at **115 the company's revenues and net income for the years 1985 through 1988. They are as follows:

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	1985	1986	1987	1988
GROSS REVENUE	$2,249.3	$1,921.2	$1,836.3	$2,273.9
NET INCOME	$ 113.2	$ 45.4	$ 44.3	$1,475.4

(EXPRESSED IN MILLIONS)

Def's Ex EEE at 3, Ex FFF at 3.)

From the above figures, it is apparent that Pennzoil's gross income in 1988 was only 24 percent higher than 1987 and almost the same as the gross income in 1985. However, the net total income for the company was 33.3 times greater in 1988 than in 1987, more than a 3,200 percent increase over the prior year. The earnings per share reported in the same exhibits show that the amount per share was 5,300 percent greater. These increases result in a company-wide "distortion" that, using Pennzoil's logic, cannot be justified by any state in which the company does business. But the fact of the matter is the unitary business received more income than its operations normally produce. Because this income was earned by the whole company, it must be apportioned to every state in which it conducts business. In this light, the 3,200 percent increase in total net income is significantly greater than the 1,877 percent "distortion" Pennzoil calculates for Oregon. Although the net income in 1988 was extraordinary, there is nothing inherently unfair in apportioning it. As noted above, except for the unitary business, there would have been no Getty contract.

Pennzoil argues that even if the settlement proceeds are business income, the court cannot justify attributing $11.3 million income to instate activities that actually operated at a loss. (Ptf's Rely Brief at 6.) This argument attacks the unitary business principle on two points. First, it assumes that separate accounting is accurate when the very reason for adopting the unitary principle was recognition that it is not. It has long been established that separate accounting on a geographical or transactional basis may not reflect the true economics of an integrated business in any particular jurisdiction.

Second, it assumes that extraordinary transactions can be severed from the unitary business. This assumption ****116** would unravel the unitary principle. If a unitary business operated at a loss overall, but one state could identify an extraordinary single transaction or series of transactions in that state which resulted in a gain, would that state be justified in separately taxing the gain? How large or small must such transactions be to justify separate accounting? If specific transactions were taxed by one or more states, how would this affect the losses apportionable to other states? These are unanswerable questions whose very asking suggests that this approach is contrary to accepted principles of interstate taxation.

***10** In summary, it is undisputed that Pennzoil is a unitary business involving a flow of value interstate that cannot be precisely measured. It is undisputed that Pennzoil does business in Oregon and therefore its business income is apportionable to Oregon. Finally, it is undisputed that Oregon's three factor formula fairly reflects the way in which income is earned by Pennzoil. These undisputed facts lead to an indisputable conclusion: Pennzoil's business income is taxable in part by Oregon.

The court has found that the income in question had its source in the Getty contract and that the Getty contract was created in the regular course of Pennzoil's business. Therefore, the income is business income as defined by ORS 314.610(1) and is apportionable.

The second issue that must be addressed by the court is whether the gross proceeds from the financial instruments involved are includible in the denominator of the sale factor. Pennzoil claims that this issue is controlled by *Sherwin-Williams Co. v. Dept. of Rev.*, 14 OTR 384 (1998), aff'd. 329 Or 599, 996 P.2d 500

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(1999). The court agrees.

Judgment will be entered consistent with this Opinion. Costs to neither party.

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STATE OF SOUTH CAROLINA
ADMINISTRATIVE LAW COURT

Duke Energy Corporation, Petitioner, vs. South Carolina Department of Revenue, Respondent,	)	Docket No. 10-ALJ-17-0270-CC

Memorandum in Reply to the Response of Duke Energy Opposing the Motion for Summary Judgment by the Department of Revenue and Memorandum Objecting to the Grant of the Cross-Motion for Summary Judgment by Duke Energy

The South Carolina Department of Revenue (the "Department" or "DOR")[1] submits this memorandum in reply to the opposition to summary judgment ("Duke Energy Response") filed by Duke Energy Corporation ("Duke Energy" or the "Company") and also in response to the cross-motion for summary judgment filed by Duke Energy pursuant to Rules of Procedure for the Administrative Law Court ("ALC") 19 and 68 and South Carolina Rule of Civil Procedure 56. As explained more fully below and in the supporting memorandum filed by the Department on April 20, 2012 ("Supporting Memorandum" or "DOR Supp. Mem."), the

[1] Because this case encompasses the years 1978-2001 (the "Periods at Issue"), the South Carolina Tax Commission was the governing authority for some of these years. But since the Department acceded to the duties and responsibilities of the Tax Commission, the terms Department or DOR also will be used to refer to the Commission unless a distinction between the specific names is appropriate.

Department is entitled to summary judgment on the three issues raised in the summary judgment motion and Duke Energy's cross-motion should be denied.

1. The amended returns for the Closed Periods at Issue are not timely.

For the reasons set forth below and in the Supplemental Memorandum, the Department is entitled to summary judgment with respect to the refund claims filed by Duke Energy for all tax years ending prior to 1994.

A. Duke Energy's arguments regarding the effect of the waiver form avoid any substantive discussion of the refund statutes in effect during the pre-1995 years, statutes that the Supreme Court has held must be "strictly complied with."

(1) *Duke Energy's entire basis for claiming that its pre-1994 refund claims are timely is the execution of Forms FS-43 regarding assessments, even though that interpretation is not supported by statutory or administrative authority for any years prior to 1995.*

Duke Energy's whole argument against the grant of summary judgment in favor of the Department concerning the pre-1994 refund claims hinges upon its argument that the myriad Forms FS-43 executed in this case allowed it additional time to file a claim for refund, an extension that would run for more than 20 years in some cases. *See* Duke Energy Response p.19. Duke Energy never discusses the particular refund statutes applicable during the Periods at Issue,[2] but simply contends that any refund limitation periods were waived through execution of the Forms FS-43. But much of the taxpayer's argument for affording it the benefit of

[2] As used in the Supporting Memorandum and here, the term "Periods at Issue" refers to the years 1978-2001, and the term "Closed Periods at Issue" refers to the years 1978-1993.

any extensions for the Closed Periods at Issue hinges upon post-1994 law while ignoring certain settled legal principles involving refund claims.

The Department should prevail on this issue because a taxpayer must strictly comply with the provisions of a refund statute. *Asmer v. Livingston*, 225 S.C. 341, 82 S.E.2d 465, 466 (1954);[3] *C. W. Matthews Contracting Co., Inc. v. S. Carolina Tax Comm'n*, 267 S.C. 548, 554, 230 S.E.2d 223, 226 (1976) (a tax refund claim is created by statute and is not in the nature of a debt collection claim). *See generally* DOR Supp. Mem. pp.18-20 (discussing refund issues). This Court repeatedly has applied these principles. *See generally id.* The Department explained in the Supporting Memorandum why it was precluded from granting extensions of time in which to file refund claims prior to 1995. DOR Supp. Mem. Part 1, pp.9-28. Therefore, the Department could not under any circumstances agree to extend the time for filing refund claims prior to 1995 and the question of whether the taxpayer could make these untimely refund claims for the Closed Periods at Issue is a question of law.

Duke Energy contends that Form FS-43 eliminates the statutory refund limitations. But Department employees cannot change the procedure authorized by the legislature for obtaining a refund. *See TNS Mills, Inc. v. S. Carolina Dept. of Rev.*, 331 S.C. 611, 621, 503 S.E.2d 471, 476-77 (1998). ("[I]n fact, the only inference arising from the legislative history is that only the General Assembly

[3] Thus, contrary to Duke Energy's argument, *see* Duke Energy Response p.16, the refund limitations period essentially is jurisdictional in nature in that neither the Department nor a court may grant a refund except on the terms set forth in the statute.

may extend the application deadline."); *Asmer*, 225 S.C. at 343-44, 82 S.E.2d at 466; *see also Guar. Bank & Trust Co. v. S. Carolina Tax Comm'n*, 254 S.C. 82, 90-91, 173 S.E.2d 367, 371 (1970) (holding that circuit court erred in extending the time periods under the statute because that is a legislative and not a judicial function). Thus, no employee of the Department could waive or extend a refund period except to the extent authorized by the governing statute. *See, e.g., Anon. Taxpayer v. S. Carolina Dep't of Rev.*, No. 01-ALJ-17-0105, 2001 WL 904045 *4 n.7 (S.C. Admin. L.J. Div. June 29, 2001) (Geathers) (denying refund claim based upon allegedly erroneous instructions and citing *U.S. v. Garbutt Oil Co.*, 302 U.S. 528, 534, 535 (1938) for proposition that "officer of the government has no power to waive statute of limitations and Commissioner cannot consider untimely filed returns"). What the Department employees may have thought regarding the purpose of Form FS-43 when the forms were executed is not pertinent. *TNS Mills, Inc.* 331 S.C. at 521-22, 503 S.E.2d at 477 ("Although [the employee] believed the Department had the authority to grant retroactive exemptions, and exemptions may have been granted under this erroneous view, neither the Commission nor the courts are bound by his erroneous interpretation.").

Duke Energy also erroneously contends that, "[f]or years, the Department advised taxpayers that it had in place a policy to execute waiver agreements extending the statute of limitations for both assessments and refunds." Duke Energy Response p.12. But that assertion is supported in part by reference to South Carolina Revenue Procedures Bulletin No. 00-3, 2000 WL 355255979

(Dec. 4, 2000) [Exhibit A], which was issued in 2000 and which was based upon the Revenue Procedures Act of 1995 ("RPA"). As fully explained in the supporting memorandum, the law pertaining to refund claims and extensions of time to claim refunds changed drastically in 1995. *See generally* DOR Supp. Mem. pp.20-21 (discussing changes made by the Revenue Procedures Act of 1995 ("RPA")). Revenue Procedure 00-3 does not assist the taxpayer's arguments for years prior to 1995.[4] The affidavits of Marvin Davant and the testimony of Joseph Southard also do not assist the taxpayer's arguments for the reason that a Department employee's erroneous understanding of the statute, even if acted upon, does not bind the Department if that understanding is not consistent with the statutory framework.[5] *TNS Mills, Inc.* 331 S.C. at 521-22, 503 S.E.2d at 477.

Duke Energy further states that Form FS-43 extended the time for filing a refund claim prior to 1995. *See* Duke Energy Response p.12. But the form is entitled "Consent to Extend the Time to Assess Tax" and, at least prior to 1995, was based upon section 12-54-80, which governs the time period in which the Department could assess taxes. Section 12-54-80 says nothing about refunds or

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[4] Duke Energy also makes an argument based on language in Revenue Procedure 00-3 that it is the Department's "longstanding administrative position" that a waiver of the assessment limitations period will also be treated as a extension of time for filing a claim for refund." S.C. Rev. Proc. 00-3. But that "longstanding administrative position" traces back to issuance of Revenue Procedure 95-5 in 1995, which addressed the many changes to refunds enacted by the RPA. Notably, Revenue Procedure 95-5 omits any language about "longstanding administrative precedent" in its discussion of the extension issue. *See* S.C. Rev. Proc. 95-5, 1995 WL 17817640 *3 (1995) [Exhibit B].

[5] Also, neither Mr. Davant nor Mr. Anderson state that they were involved in drafting or preparing Form FS-43.

extensions of time to file refund claims.[6] *See generally* DOR Supp. Mem. pp.9-11. Therefore, section 12-54-80 provides no authority for the Department prior to 1995 to extend the time in which Duke Energy could file refund claims by executing Form FS-43.

Duke Energy apparently contends that the absence of the word refund from section 12-54-80 means that the rights granted by Form FS-43 were unlimited. *See* Duke Energy Response p.12. It also contends that because Form FS-43 does not reference South Carolina Code Section 12-54-30, that statute does not apply either. *Id.* However, Duke Energy points to no statutory authority whatsoever for the Department to grant a refund claim outside of the time periods imposed by the pertinent refund statutes prior to 1995.[7] Again, the taxpayer's entire argument boils down to an assertion that Form FS-43 extended the time to make refund claims no matter the applicable statutory language. But because section 12-54-80 does not reference or authorize refund claims, the taxpayer's only available remedy for the years before 1994 is section 12-54-30.[8]

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[6] Moreover, the point made by Duke Energy regarding use of Form FS-43 to reference a statute that had been repealed further supports the point made by Ronald Urban that the form appears to have been adopted by the Field Services division (hence the "FS" designation) and was never formally approved as a matter of policy by the Commission or the Department. [*See* Affidavit of Ronald W. Urban ¶19 [Exhibit C].]

[7] As previously explained, the General Assembly afforded the Department the ability to extend the time to make refund claims for years after 1994 as part of the RPA.

[8] In this context, Mr. Davant states his understanding that Form FS-43 allowed the Department to issue refunds of overpaid tax even if the claim for refund otherwise would not be timely. [Affidavit of Marvin Davant ¶15 [Exhibit D to Duke Energy Response].]. That is a correct statement because South Carolina Code Sections 12-7-2240, *see* discussion *infra* Part 1.B.(3), and section 12-54-30 permitted such refunds if

Duke Energy also makes much of the Department's acknowledgement that Forms FS-43 would extend the time period for claiming a refund for years that were open on or after the effective date of the RPA. Duke Energy Response p.13. It contends that because the Department agrees that Form FS-43 had that effect for 1995 and later, it must have had that effect before 1995. But that argument ignores the substantial and wholesale changes that were enacted as part of the RPA. The form operates to extend the time for both assessment and refunds for 1995 and later because the Department acknowledged in Revenue Procedure 95-5 that, based on changes made by the RPA, extensions of time to assess tax would also extend the time to request refunds. *See* S.C. Rev. Proc. 95-5, 1995 WL 17817640 *3 (1995) [Exhibit B]. Applying these pertinent statutes and controlling legal principles hardly is a "selective application of South Carolina law." Duke Energy Response p.13.

Duke Energy's argument is that Department employees could, based on a mistaken and erroneous understanding of their authority, bind the general fund of this state to pay refund claims more than 25 years after the fact. The Supreme Court rejected that assertion in *TNS Mills*. The taxpayer attempts to distinguish the tax related cases cited by the Department based upon certain factual differences between those cases and this one. This case admittedly is unique given the taxpayers claim on the general fund based on a return filed more than 30 years ago

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the examination was otherwise timely. As explained elsewhere, Form FS-43 did not and could not extend the time for the taxpayer to make a refund claim.

and 23 years before a refund claim was filed. But the authority to grant refunds can only be granted by statute, and Duke Energy can point to nothing prior to 1995 giving the Department that authority. Thus, there is no factual dispute concerning Duke Energy's ability to claim refunds prior to 1994 based on Form FS-43 and the Department is entitled to partial summary judgment on those years.

(2) ***Duke Energy's statute of limitations analysis is not helpful because it draws upon cases decided outside of the taxation context, a crucial distinction.***

Duke Energy expends much analysis contending that the refund limitations periods are in the nature of statutes of limitations and, as such, may be waived.[9] In essence, this is a claim that the Department may be estopped from asserting a refund limitations period or that the refund limitations period is subject to equitable tolling. As explained more fully below, *see* discussion *infra* Part B.(1) & (2), this position has been rejected by the United States Supreme Court and by courts of this state. For these same reasons, Duke Energy's argument regarding waiver of general statutes of limitation should be rejected.

In the only general statute of limitations case actually cited by Duke Energy that involves the Department, the taxpayer's refund claim was based on the

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[9] Duke Energy points to a statement in *Hercules v. S. Carolina Tax Comm'n*, 274 S.C. 137, 262 S.E.2d 45 (1980), that a "statute of limitations affects the remedy and not the right." *Hercules*, 274 S.C. at 143, 262 S.E.2d at 48. But *Hercules* was addressing not a refund limitations period, but the timeliness of an assessment based on a tolling process expressly provided for by the governing statute. *See id.*, 274 S.C. at 140, 262 S.E.2d at 47; *see also* discussion *infra* Part 1.B.(3) (discussing *inter alia* S.C. Code Ann. §12-7-2220). In contrast to the situation in *Hercules*, there is no tolling or other extension provided by statute for the Closed Periods at Issue.

contention that his right to retirement benefits was in the nature of a contract. *Anon. Taxpayer v. S. Carolina Dept. of Rev.*, 377 S.C. 425, 431-32, 661 S.E.2d 73, 76 (2008). The Supreme Court's discussion of the statute of limitations in that case was predicated upon the taxpayer's argument that there "was a contract providing for continuing performance, thus the limitations period began anew each year." *Id.* at 438, 661 S.E.2d at 80. The Court noted long ago that statutes of limitations could be waived with respect to actions based on contract. *See Heyward v. S. Carolina Tax Comm'n*, 240 S.C. 347, 351, 126 S.E.2d 15, 17 (1962) ("We have held that the State may be subject to the doctrine of estoppel in its contractual relations."). The Court has not held that refund claims are in the nature of a contract and, in fact, has held the opposite. *See id; see also C. W. Matthews Contracting Co.*, 267 S.C. at 554, 230 S.E.2d at 226 (a tax refund claim is created by statute and is not in the nature of a debt collection claim). More to the point, the Court has not ruled that tax refund limitations periods may be waived by the Department or its employees and, to the contrary, has ruled that refund statutes must be strictly applied. *See* discussion *supra* Part 1.A.(1).

The essence of Duke Energy's argument is that the Department may waive the enforcement of the applicable limitations period for years prior to 1994 even if those years had expired. *See* Duke Energy Response p.19. It makes this argument even though it recognizes that the "authority cited by the Department simply stands for the proposition that a statute of limitations is closed if the applicable limitations period expired without the presence of a written agreement for the

extension of such period." That is a correct statement of the law. *Yamshak v. S. Carolina Dep't of Rev.*, No. 96-ALJ-17-0086, 1996 WL 909349 (S.C. Admin. L.J. Div. June 7, 1996) (Geathers). *See generally* DOR Supp. Mem. p.18 (discussing inability to revive expired refund limitations period). Duke Energy's argument that the Department could waive enforcement of the statute of limitations is, however, inconsistent with that proposition and should be denied.

Duke Energy's waiver contention is inconsistent with the judicially-recognized inability of the Department to grant refunds except in compliance with the pertinent statutes governing refund claims.[10] Furthermore, although it expands the situations and time frames for claiming refunds, the RPA provides that, for 1995 and later, [a] taxpayer may waive his rights under [Chapter 60]" and that the "Department may extend time limitations." S.C. Code Ann. § 12-60-40. In other words, even in the post-1994 modern era, waiver is only authorized by statute on the part of the taxpayer whereas the Department may only extend the refund periods. The ability to extend necessarily contemplates action taken before and not after the pertinent time period concludes. This conclusion is consistent with South Carolina Code Section 12-60-470(H), which permits a taxpayer to amend a refund claim "before, but not after, the expiration of the time for filing the claim for

[10] Duke Energy states that the Department asserts that "extensions of time for assessing taxes did not extend the time for filing a refund prior to the RPA" and does so "without citing to a single statute, regulation, rule or other authority." Duke Energy Response p.19. The Department's discussion of the pertinent authority may readily be found in the pages preceding the isolated statement cited by Duke Energy, particularly on pages 11 and 12 of the Supplemental Memorandum.

refund." It also is consistent with the proposition discussed above that a closed refund limitations period may not be reopened.

(3) ***Duke Energy's factual recitation is incomplete.***

At the outset of its memorandum, Duke Energy makes a number of assertions regarding the history of this case that are incomplete. It certainly is true that the examination of this taxpayer by South Carolina remained open for many years. But that status was driven by the fact that Duke Energy was under examination "during much of the 1980s" by the IRS regarding the tax treatment of Duke Energy's sale of the plant and facilities located in Cherokee County, South Carolina that were going to be used for the construction of the Catawba Nuclear Station.[11] Ultimately, that audit was concluded[12] and, in fact, federal and state refunds were issued to Duke Energy on that basis.[13] *See* Duke Energy Response p.6 n.2. Thus, the extensions of time in which the Department could not assess taxes did not benefit just the Department because the taxpayer ultimately received a refund.[14] In fact, Duke Energy's representative testified that delaying the South Carolina examination would benefit the company by "having to audit the years once for South Carolina instead of multiple times." [Monroe Dep. 47:3-9 [Exhibit

[11] [*See* T. Cooper Monroe Dep. 45:19-22; 46:14-47:3 [Exhibit D].]

[12] [*See* Exhibit E (April 19, 1991 letter notifying Department that the years 1978-1983 had been settled).]

[13] [*See* Exhibit F (Department notice regarding amount of refund).]

[14] Duke Energy states that Department appears to have abandoned the settlement claim raised in the Department's Amended Prehearing Statement. That is not correct. The Department has not raised that issue as part of its motion for summary judgment, but the issue has not been abandoned at this time.

D].] Among other things, this would have conserved Duke Energy's resources. [*See* Monroe Dep. 47:10-48:20 [Exhibit D].][15]

This mutual benefit also is demonstrated by items disclosed in discovery that are not mentioned by Duke Energy. In file notes prepared by Randy Wilson, the examining agent, Duke Energy "was signing waivers annually as he said that it would be easier to settle all issues when IRS audit finished the appeals process, etc." [Monroe Dep. 51:20-52:8 [Exhibit D] & Notes [Exhibit G].] By correspondence near the end of the refund period and dated December 16, 1999 from Duke Energy's counsel, Burnet R. Maybank, [Exhibit H,] Duke Energy suggested there was no urgency in completing the audit[16] and requested an extension of time based on his vacation plans[17] in a letter omitted by Duke Energy from the attachments to its responsive memorandum. [*See* Monroe Dep. 50:24-51:14 [Exhibit D].] And in correspondence near the beginning of the examination process, Duke Energy apparently became concerned that they had not received the consent form and enclosed a signed and modified copy of the previous consent form. [Exhibit I.] In short, it was not only the Department that sought to extend the

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[15] [*See also* Monroe Dep. 63:18-64:19 [Exhibit D] (noting in response to question from Duke Energy counsel that an employee "[m]ost likely" would be "required to spend 100 percent of their time on the South Carolina audit for the week that the South Carolina auditor was on site.").]

[16] "I know that you have had a very rough year and have much bigger fish to fry at the current time than finishing the audit report, so we would very much appreciate your providing us with another extension." [Exhibit H.]

[17] "I will be knocking off for vacation next Tuesday, so for selfish reasons, I would appreciate your providing us with an extension in the next few days." [Exhibit H.]

assessment period and Duke Energy was not a passive participant doing no more than "cooperatively and patiently accomodat[ing] the Department's serial requests to extend the audit ...." Duke Energy Response p.3.

Duke Energy goes on to state that it "agreed to the waivers because the Department represented verbally and in writing that the statute of limitations was extended for both tax assessments and tax refund claims." Duke Energy Response p.4. As explained above, for years prior to 1995, any statement made by a Department employee along those lines would be inconsistent with the governing statutes and, thus, outside of that employee's authority. Moreover, the citation to the deposition testimony by Jan Urban does not support the Department's assertion. Specifically, in the portion of Ms. Urban's testimony referenced by Duke Energy, she was discussing a letter from Mr. Maybank discussing the impact of signing a Form 870, not a Form FS-43. [Urban Dep. 69:23-70:5 [Exhibit J] & Letter [Exhibit K].] It appears that a Form 870 never was signed with respect to the corporate income tax examination. [*See* Urban Dep. 69:15-25 [Exhibit J] & email [Exhibit L] (Harley Priesmeyer states that "we could do without the SC870 for income/license fee"). Finally, Ms. Urban simply was testifying that Form SC870—not Form FS-43—would have held open periods otherwise open for review.[18] That statement does not in any way amount to a representation by the

[18] Q: And that document [Form SC870] would have held open the periods for Duke to file refunds; is that correct?

A: Would have held open certain periods.

Department that Forms FS-43 extended the refund limitations period for years prior to 1994.

Duke Energy states that, "[f]or years, [it] discussed with the Department in emails and in writing that Duke Energy intended to file the amended returns." Duke Energy Response p.6. But the reference to Ms. Urban's deposition does not support that assertion because it relates only to the document that was being discussed in the deposition. Ms. Urban further testified that, to her recollection, Duke Energy explained that it sought to file refund claims for credits and adjustments, such as tax credit incentives recruiting industry and investment in South Carolina, not for the changes set forth in the amended returns for the Periods at Issue. [Urban Dep. 63:17-64:5 [Exhibit J].] Harley Priesmeyer from Duke Energy stated that the company was "planning on filing amended returns for some credits and other deductions/adjustments not previously taken for these years." [Urban Dep. 65:9-12 [Exhibit J] & email [Exhibit M].] The phrase "some credits and other deductions/adjustments" hardly sounds like the wholesale change in the company's accounting methods for apportionment. And Mr. Maybank's March 20, 2002 letter stated that "Duke is examining the possibility of filing amended returns for the purposes of claiming tax incentives, as well as possibly other adjustments." [Exhibit N.] This language sounds almost exactly like Mr.

Q. Otherwise open periods?

A. Exactly.

[Urban Dep. 70:1-5 [Exhibit J].]

Priesmeyer's language that led Ms. Urban to conclude that Duke Energy was only looking to take additional incentives and credits, not make a wholesale change to the company's accounting methods.

Finally, Duke Energy complains[19] about the amount of $63,180,088 identified by the Department. *See* Duke Energy Response p.7. It states that the "refund calculations set forth in the Department's Memorandum are incorrect." *Id.* However, it does not correct those allegedly erroneous calculations. But given the amounts at issue here, totaling more than $125 million with consideration of interest, [Exhibit F to DOR Supp. Mem.,] it is unlikely that the Department's calculation is materially incorrect for purposes of assessing the impact of the issues in the motion for summary judgment.

B. Duke Energy's remaining arguments regarding principles applicable to the refund procedures at issue for the tax years prior to 1994 are not supported by the decisions of the South Carolina Supreme Court, the South Carolina Court of Appeals, or this Court.

(1) *The Department is not subject to estoppel and Duke Energy's own case citations establish that principle as a matter of law.*

As explained above and in the supporting memorandum, the Department is not subject to estoppel. *Texaco, Inc. v. Wasson*, 269 S.C. 255, 265, 237 S.E.2d 75, 79 (1977); *Heyward*, 240 S.C. at 352, 126 S.E.2d at 18 (1962). *See generally* DOR

[19] Duke Energy also contends that there are genuine issues of material fact just because the Department did not sign the taxpayer's proposed stipulations. Duke Energy Response p.7. That is not a conclusion that can fairly be drawn from the absence of stipulations at this stage. This "conclusion" is of the same nature as the argument that there are material facts in dispute because the Department retained an expert regarding electricity. *See* discussion *infra* p.32.

Supp. Mem. pp.18-20 (discussing estoppel issues). In *Texaco*, the Court held that the Department was not estopped from assessing additional taxes based on the use of an improper accounting method even though Department employees had expressly and in writing authorized the taxpayer to use that method "until such time as the South Carolina Tax Commission grants permission to change such method." *Texaco*, 269 S.C. at 264-65, 237 S.E.2d at 79.

In *Heyward*, the taxpayer argued that the Department was estopped from directing the taxpayer to include certain profit as income in the year of the taxpayer's death "because of acquiescence in and approval of the taxpayer's election of the installment method of reporting profit ...." *Heyward*, 240 S.C. at 351, 126 S.E.2d at 17. The Court rejected that argument, holding instead that "estoppel will not be applied to deprive the government of the due exercise of its police power, or ***to effect public revenues*** or property rights, or to frustrate the purpose of its laws or thwart its public policy." *Id.* (emphasis added) (citing *Powell v. Bd. of Com'rs of Police Ins. & Annuity Fund of State*, 210 S.C. 136, 41 S.E.2d 780 (1947)).

In yet another case, a taxpayer contended that the Department had the authority to grant a property tax exemption retroactively. *TNS Mills, Inc.*, 331 S.C. at 621, 503 S.E.2d at 476-77. This contention was based in part on a memorandum prepared and issued by a Department employee opining that a recently-enacted statute gave the Department authority to accept exemption applications at any time. *Id.* The Court rejected this contention, holding instead that "[a]lthough [the

employee] believed the Department had the authority to grant retroactive exemptions, and exemptions may have been granted under this erroneous view, neither the Commission nor the courts are bound by his erroneous interpretation." *Id.* at 521-22, 503 S.E.2d at 477.

Thus, the Department is not estopped from invoking the correct refund limitations period even if Department employees did believe they had the authority to allow the taxpayer to extend the time in which a claim for refund could be filed. The execution of Forms FS-43 by Department employees can provide the taxpayer with no greater remedies than those provided by the governing statutes for refund claims and the like. To conclude otherwise would be to permit auditors to allow the general fund of this state to be diminished without the consent of the General Assembly. This Court has recognized the problems inherent in the position now articulated by Duke Energy. *See Danzie v S. Carolina Dep't of Rev.*, No. 7-ALJ-17-0327, 2008 WL 2127919 (S.C. Admin. Law Ct. Apr. 21, 2008) (Geathers). As such, this Court also has recognized and enforced the Supreme Court's holdings regarding estoppel. *See, e.g., Anon. Taxpayer v S. Carolina Dep't of Rev.*, No. 00-ALJ-17-0668, 2001 WL 855849, *6 (S.C. Admin. L.J. Div. July 5, 2001) (Stevens) (determining that there are no equitable exceptions to refund statute and that estoppel is not applicable against the Department) (citing *S. Carolina Coastal Council v. Vogel*, 292 S.C. 449, 357 S.E.2d 187 (Ct. App. 1987). ("The public cannot be estopped ... by the

unauthorized or erroneous conduct or statements of its officers or agents which have been relied on by a third party to his detriment.")).

The authority Duke Energy itself cited supports the Department's position that it is not estopped from rejecting actions taken by its employees that are not authorized by statute. The taxpayer cited *Quail Hill, LLC v. County of Richland*, 387 S.C. 223, 236, 692 S.E.2d 499, 506 (2010) and quoted the following language from that case: "A governmental body is not immune from the application of the doctrine of estoppel where its officers of agents act within the proper scope of their authority." Duke Energy Response p.22. However, Duke Energy only quoted the first part of the pertinent language and failed to provide the entire context of the cited passage, which was block indented by the Court as follows:

> A governmental body is not immune from the application of the doctrine of estoppel *where its officers or agents act within the proper scope of their authority ...* ***The public cannot be estopped, however, by the unauthorized or erroneous conduct or statements of its officers or agents which have been relied on by a third party to his detriment.***

Quail Hill, 387 S.C. at 236, 692 S.E.2d at 506 (italics in original) (quoting *DeStefano v. City of Charleston*, 304 S.C. 250, 257-58, 403 S.E.2d 648, 653 (1991)). That passage came by way of support for the Court's statement at the beginning of the paragraph: "As a general rule, estoppel does not lie against the government to prevent the due exercise of its police power or to thwart the application of public policy." *Id.* (quotation marks omitted). And this entire analysis was set forth in support of the Court's ultimate holding: "For reasons ...

discussed [in the opinion], we believe the Court of Appeals erred in reversing the circuit court's grant of summary judgment to County as to Quail Hill's claim of equitable estoppel." *Id.*, 387 S.C. at 237, 692 S.E.2d at 506.

In other words, the Supreme Court in *Quail Hill* affirmed that the government was not estopped from contesting erroneous statements made by its staff. *See id.*, 387 S.C. at 238, 692 S.E.2d at 507 ("[W]e agree with County's argument that the RU zoning classification was a mistaken statement of law and, thus, could not be used to estop County from enforcing it."). That holding is entirely consistent with and supports the holdings of *Texaco*, *Heyward*, and *TNS Mills* discussed above. *See id.*, 387 S.C. at 236, 692 S.E.2d at 506 ("[E]stoppel will not lie against a government entity where a government employee gives erroneous information in contradiction of statute.") (quotation marks omitted). The *Quail Hill* decision in fact relies on the same rationale stated by the Court in *Heyward* that the government cannot be estopped from exercising the police power. *Compare id.*, 387 S.C. at 236, 692 S.E.2d at 506 (discussing police power rationale for not applying estoppel to governmental entities) *with Heyward*, 240 S.C. at 351, 126 S.E.2d at 17 (holding that "estoppel will not be applied to deprive the government of the due exercise of its police power, or to effect public revenues or property rights ...."). In sum, although cited by Duke Energy, the *Quail Hill* decision supports—not refutes—the Department's position that it is not bound by estoppel.

(2) ***For generally the same reasons that it is not subject to estoppel, the Department also is not subject to equitable tolling.***

The Department also is not subject to equitable tolling. *Anon. Taxpayer v S.C. Dep't Rev.*, No. 01-ALJ-17-0347, 2002 WL 385115 (S.C. Admin. L.J. Div. Feb. 13, 2002) (Anderson) ("Section 12-54-85(F)(1) provides for no hardship or equitable exceptions to its time limitations."); *see also Anon. Taxpayer*, No. 00-ALJ-17-0668, *6 (determining that there are no equitable exceptions to refund statute). These decisions are supported by the rationale that revenue statutes do not incorporate these equitable limitations on their application. *See United States v. Brockamp*, 519 U.S. 347, 352 (1997); *see also* S.C. Rev. Proc. 95-5 *1 [Exhibit B] ("Although the statute of limitations is arbitrary and can cause hardships, its application is designed to be neutral. As noted by the Supreme Court in *Rothensies v. Electric Storage Battery Co.*, 329 U.S. 296 (1946), the 'statute of limitation is an almost indispensable element of fairness as well as of practical administration of income tax policy.'").

Duke Energy cites to decisions by the Supreme Court and the Court of Appeals as part of successive appeals in a single case in support of its assertion that equitable tolling applies. *See* Duke Energy Response p.23 (citing *Hooper v. Ebenezer Sr. Svcs. & Rehab Ctr.*, 386 S.C. 108, 687 S.E.2d 29 (2009); *Hooper v. Ebenezer Sr. Svcs. & Rehab Ctr*, 377 S.C. 217, 659 S.E.2d 213 (Ct. App. 2008)). None of these cases involve the Department or taxpayers or refund claims and,

thus, given the unique nature of the revenue-related issues in this case, provide minimal direction to this Court in adjudicating this matter.

In fact, in the only South Carolina appellate decision remotely touching upon taxation issues and equitable estoppel, the Court of Appeals held that equitable estoppel did not apply to bar a county from asserting the statute of limitations as a defense to refunding admissions fees paid in connection with bingo games. *Am. Legion Post 15 v. Horry County*, 381 S.C. 576, 583, 674 S.E.2d 181, 184 (Ct. App. 2009). The court rejected the taxpayer's argument that the statute of limitations should be tolled, holding instead that a letter requesting a refund did not operate to toll the limitations period because "[n]othing presented the [taxpayers] from learning of the governing statutes, as we find is required for due diligence." *Id.*[20]

For the same reasons, Duke Energy is not entitled to a benefit from equitable tolling. The doctrine has not been applied against the Department in a tax context by this Court or by appellate courts in this state and there is no basis for departing from that precedent in this case. As stated by the Court of Appeals, Duke Energy could have referenced the governing refund statutes and learned that

[20] The Court of Appeals also rejected the taxpayer's claim that the County was estopped from raising the statute of limitations on the basis that "[c]itizens are presumed to know the law and are charged with exercising reasonable care to protect their interests" and that "[e]stoppel will not lie against a governmental entity when a government employee gives erroneous information in contradiction of statute." *Am. Legion Post 15*, 381 S.C. at 584, 674 S.E.2d at 185.

Department employees cannot extend the time periods set forth in the applicable refund statutes. *See Am. Legion Post 15*, 381 S.C. at 583, 674 S.E.2d at 184.

(3) *Duke Energy's arguments about federal adjustments with respect to the 1978-1992 tax years do not permit them to file an untimely refund claim for those years.*

Duke Energy erroneously argues that because South Carolina Code Section 12-54-85(D)(1) was not in effect during the 1978-1982 tax years, federal adjustments operated to reopen those years for all items, not just those listed on the federal report. Duke Energy Response p.24. The Court does not need to resolve this issue because the 1978-1982 tax years do not comply with the refund periods set forth in the applicable statutes.

Moreover, South Carolina Code Section 12-54-140, which was enacted in 1985, required corporations to notify the Department of any changes made by the IRS. That statute expressly notes that the time limitation for assessment or refund of taxes does not apply to underpayments and overpayments "resulting from changes in income made by the [IRS]." S.C. Code Ann. § 12-54-140. In other words, the time periods reopened only for the changes made by the IRS. But if Duke Energy is correct that the issue was governed by the statutes actually in effect during the years in question, the issue would have been controlled by South Carolina Code Section 12-7-2230, which was in effect until section 12-54-140 was adopted in 1985.

Section 12-7-2230 also required taxpayers to notify the Commission of any federal examination of its books and records within 30 days after it had or should

have had knowledge of any such examination. S.C. Code Ann. § 12-7-2230 [Exhibit O, Tab 3.] The statute also required that the taxpayer notify the Commission if it executed a waiver of the federal limitations period. *Id.* Failure to notify the Department of the federal examination or of the execution of the waiver would "automatically suspend the limitations set forth in § 12-7-2220 ... until [90] days after the Tax Commission receives notice in writing." *Id.* It must be noted that the limitations period of South Carolina Code Section 12-7-2220 [Exhibit O, Tab 2] referenced by section 12-7-2230 was directed only toward the assessment of additional taxes with three years after the return was filed or due to be filed. Section 12-7-2220 made no reference to refunds, an omission that by comparison to section 12-54-140 suggests that the General Assembly did not wish to provide for such refunds prior to enacting section 12-54-140 in 1985.

Thus, during the tax years 1978-1992 and in keeping with the restrictive refund periods applicable prior to 1995, section 12-7-2230 only extended the period of time for assessing additional taxes against a taxpayer based on a federal examination. It did not address or extend the time period for filing refund claims. Limited authority to make refunds in situations like these were granted to the Commission by another statute, which stated that "[i]f the Commission discover[ed] from the examination of the return or otherwise that the income tax ... is in excess of the amount legally due," it could refund the appropriate amount to the taxpayer. S.C. Code Ann. § 12-7-2240 [Exhibit O, Tab 4]. Section 12-7-2240 provides the same limited remedy provided by section 12-54-30 that is

discussed more fully in the Department's supporting memorandum. But it permits a taxpayer a refund only if the Department determines that it is entitled to one and a determination under section 12-54-30 is not subject to further review.

In sum, whether section 12-54-140 is applied to the years 1978-1982 or whether sections 12-7-2220 and -2230 are applied to those years, the result is the same. The federal adjustments would have reopened those years, but only for assessments regarding the adjustments proposed by the IRS. Those statutes do not afford the taxpayer the benefit of reopening those years for filing a refund claim based on any item set forth in the original return, which stands to reason given that a taxpayer would not want the Department to have the ability to assess taxes on items other than those encompassed within the federal adjustments.

Although section 12-7-2240, like section 12-54-30, permitted the Commission, upon examination, to refund taxes in excess of the amount legally due, Duke Energy has received the benefit of any review that it was entitled to under that statute or section 12-54-30.[21] While Duke Energy understandably is unhappy with the results of that review, it nevertheless is entitled to no further

[21] Further supporting the argument advanced by the Department in the Supporting Memorandum that the term "refund" in Form FS-43 references a refund identified by the Department during an examination, South Carolina Code Section 12-7-2210 [Exhibit O, Tab 1] in effect during those years states that if "the amount of tax found due as computed shall be less than the amount theretofore paid, the excess shall be ordered refunded by the Commission." That is, however, a duty placed on the Commission *Peoples Nat. Bank of Greenville v. S. Carolina Tax Comm'n*, 250 S.C. 187, 192, 156 S.E.2d 769, 772 (1967). The refund and review of that determination therefore would be controlled by section 12-7-2240 and is unreviewable unless the taxpayer paid its taxes under protest and instituted an appropriate refund action. *See Peoples Nat. Bank*, 250 S.C. at 190, 156 S.E.2d at 771.

review of its refund claims for the years 1978-1982—or any other tax years prior to 1995—based on the refund limitations periods imposed by the governing statutes. *Argent Lumber Co. v. Query*, 178 S.C. 1, 182 S.E. 93 (1935) (no right to judicial review of predecessor statute), *overruled on other grounds by McCall by Andrews v. Batson*, 285 S.C. 243, 329 S.E.2d 741 (1985). The 1978-1982 tax years therefore are closed against further review.

(4) ***Contrary to Duke Energy's assertion, it is not erroneous to apply the plain language of the statute governing refund claims during the years in question.***

For the reasons more fully explained in the Department's supporting memorandum, Duke Energy's refund claims for the tax years 1992 and 1993 are untimely based on the plain language of South Carolina Code Section 12-47-440. Duke Energy's argument is based on an assertion that the applicable three-year period ran from the date the return was filed using the periods set forth in section 12-54-85.[22] However, as repeatedly emphasized by the Department, section 12-54-85 did not apply before 1995.

As applicable to the years 1990 through 1994, section 12-47-440 provided that a taxpayer could file a refund claim "in writing to the Commission within a period of three years from the date the license fee or tax was due to have been paid, without regard to extensions of time for payment ...." As explained in the

[22] In its previous argument regarding federal adjustments, Duke Energy contended that the statutes in effect during the actual tax years must govern the status and extent of any opening of the refund limitations periods. In this argument, however, Duke Energy contends that a statute adopted after the years in question must govern the status and extent of any opening of the refund limitations period.

Department's Supporting Memorandum, for a corporate taxpayer on a calendar year like Duke Energy, the payments for the 1992 and 1993 tax years would have been due on March 15, 1993 and March 15, 1994, respectively, and the refund period under section 12-47-440 would have expired on March 15, 1996 and March 15, 1997, respectively. Because Form FS-43 referencing tax year 1992 was not executed until May 30, 1996 and Form FS-43 referencing tax year 1993 was not executed until June 20, 1997, those years expired before the form was executed and may not later be reopened. *See Guar. Bank & Trust Co. v. S. Carolina Tax Comm'n*, 254 S.C. 82, 90-91, 173 S.E.2d 367, 371 (1970) (holding that circuit court erred in extending the time periods under the statute because that is a legislative and not a judicial function); *Yamshak*, No. 96-ALJ-17-0086 (concluding that closed refund periods may not be reopened).

2. Contrary to Duke Energy's argument, there are no material facts in dispute because the Supreme Court already has held that electric utilities in general and Duke Energy in particular are engaged in the business of manufacturing.

As Duke Energy acknowledges, the three-factor formula of property, payroll, and sales must be applied by entities "whose principal business in this State is (a) manufacturing or any form of collecting, buying, assembling, or processing goods and materials within this State or (b) selling, distributing, or dealing in tangible personal property within this State." S.C. Code Ann.

§ 12-6-2250.[23] Although there is another statute providing for apportionment using gross receipts alone that the taxpayer now seeks to apply retroactively for all years back to 1978, *see* S.C. Code Ann. § 12-6-2290, that statute does not apply to taxpayers engaged in the business of manufacturing.

This Court is not, however, required to resolve that question because it already has been answered by the South Carolina Supreme Court. The Court has held that a corporation engaged in the business of generating electricity was engaged in the business of manufacturing and thereby subject to a tax imposed on manufacturers. *Columbia Ry., Gas & Elec. Co. v. Query*, 134 S.C. 319, 132 S.E. 611 (1926) ("We do not think that there is any doubt that the appellant is engaged in the business of manufacturing gas and electricity ...."). The Supreme Court reaffirmed that conclusion in 1930, holding that Duke Power, a direct predecessor of Duke Energy, was entitled to claim an exemption for manufactories—defined as a physical plant, or a place or building, where manufacturing is carried on—because it was a manufacturer. *Duke Power Co. v. Bell*, 156 S.C. 299, 152 S.E. 865 (1930) (citing *Columbia Ry., Gas & Elec. Co.*). Almost certainly because it spoke so clearly on the issue, not once but twice, the Court has not revisited the issue. Those holdings therefore remain the law of this State.

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[23] Section 12-6-2250 as applicable during the Periods at Issue requires that the sales factor be double-weighted in calculation of the apportionment formula. This section was previously designated as section 12-7-1140, which was repealed in 1995. Prior to June 12, 1995, section 12-7-1140 provided a three factor formula without the double-weighted sales factor.

Duke Energy's response to those cases is to dismiss them because they were based on the Manufacturer's Act and not the apportionment statutes. Duke Energy Response p.27. Similarly, they dismiss the Department's citation to an Attorney General's Opinion[24] as based upon property tax issues.[25] Duke Energy Response p.27. Duke Energy instead argues that a decision regarding the license tax imposed upon public utilities must govern this Court's decisions and accuses the Department of being "disingenuous at best" by arguing against the application in this case of *Consolidated Hydro Southeast, Inc. v. S. Carolina Dep't of Rev.*, No. 95-ALJ-17-0634, 1996 WL 909155 (S.C. Admin. Law J. Div. May 13, 1996) (Lee). *Id.* But the important difference is that, aside from the fact that the Supreme Court decided the *Columbia Railway* and *Duke Power* cases, those decisions address the terms "manufacturer" and "manufacturing," whereas *Consolidated Hydro* addressed the term "services" and does so in the context of the license tax applicable to public utilities only, not the apportionment statute applicable to all taxpayers.

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[24] *See* Mem. Supp. Dep't Mot. Sum. J. p.29 (citing 1970 S.C. Op. Att'y Gen. 154, Op. No. 2909, 1970 WL 12192 (June 2, 1970) [Exhibit M to DOR Supp. Mem.].

[25] Duke Energy does not mention the Department's citation, *see* Mem. Supp. Dep't Mot. Sum. J. p.29, to a prior decision of the South Carolina Tax Commission concluding that "'X' Electric and Gas" was a manufacturer because the Supreme Court had held that its predecessor was a manufacturer in the *Columbia Railway* decision. S.C. Tax Comm'n Decision P-D-532, 1985 WL 192777 (Apr. 11, 1985) [attached as Exhibit J, Tab 6 to DOR Supp. Mem.] This decision establishes agency precedent that the term "manufacturing" includes electric utilities. It also reflects, along with the Attorney General's Opinion, that the Supreme Court's holdings in the *Columbia Railway* and *Duke Power* cases have been understood for many years as conclusively answering the question of whether an electric utility is encompassed within language in a tax statute directed toward manufacturing.

Furthermore, the language of the Manufacturer's Tax Act at issue in *Columbia Railway* requires its application to this case. Specifically, the statute at issue required that "every person, firm or corporation engaged in the business of manufacturing" was subject to the tax imposed on manufacturers. 1923 S.C. Acts 12, No. 21 §11-A [Exhibit P]. And, although the tax at issue was a license tax on "the entire receipts," it was specifically imposed on "the business of manufacturing," not on "services rendered from regulated business." *See* S.C. Code Ann. §12-20-100(A)(2)(a).[26] Thus, *Consolidated Hydro* does not assist in resolving this case because it is based on different language in a different taxing framework, whereas *Columbia Railway* is based on a 1923 Act directed at manufacturers and using the same language as the apportionment statute at issue in this case. *Compare* S.C. Code Ann. § 12-6-2250 (applying to "a taxpayer whose principal business in this State is ... manufacturing") *with* 1923 S.C. Acts 12, No. 21 §11-A (applying to a taxpayer "engaged in the business of manufacturing"). The *Duke Power* case, aside from expressly deciding that the taxpayer before this Court is a manufacturer, involved the application of *Columbia Railway* to determine whether the taxpayer fell within a statute exempting "manufactories" from county taxes. *Duke Power*, 156 S.C. at 299, 152 S.E. at 868; *see* 1925 S.C. Acts 891, No. 468 §1 [Exhibit Q].

[26] The statutes discussed in *Consolidated Hydro*, sections 12-19-100 and 12-19-110, now are codified together as South Carolina Code Section 12-20-100.

The *Columbia Railway* and *Duke Power* cases therefore stand for the proposition that language in a tax statute encompassing "manufacturing" includes companies like Duke Energy that are engaged in manufacturing, generating, or producing electricity. Consequently, even if other statutes—like the license tax on public utilities—are directed toward gross receipts from services rendered by electric utilities, these two decisions establish that electric utilities nevertheless are engaged in manufacturing for purposes of South Carolina statutes directed toward manufacturers. Focusing on the actual delivery of electricity as a service in one statutory framework is not at all inconsistent with focusing on the actual generation of electricity as manufacturing in another statutory framework.[27]

This Court also should reject Duke Energy's contention that summary judgment is not appropriate because electricity is not tangible personal property. The expert retained by the Department has opined that it is tangible property. [*See* Affidavit of Glenn Robinson ¶¶12-13 [Exhibit R].] And although not binding here, courts in other states have concluded that electricity is tangible personal property, both in taxation contexts and otherwise. *See, e.g., Pub. Serv. Co. v. Dep't of Rev.*, 10CA1026, 2011 WL 4089971, **7-8 (Colo. Ct. App. Sept. 15, 2011) (holding that generating electricity is manufacturing for purposes of an exemption from

[27] Even if the treatment is inconsistent, which the Department does not concede, it is for the General Assembly to reconcile the differences in the plain language among the two statutory taxation frameworks. *See, e.g., Creech v. S. Carolina Pub. Serv. Auth.*, 200 S.C. 127, 20 S.E.2d 645, 652 (1942) ("The responsibility for the justice or wisdom of legislation rests with the Legislature, and it is the province of the courts to construe, not to make, the laws."). The issue presented here is whether Duke Energy falls within the language of the apportionment statute.

sales taxes for machinery "used in Colorado directly and predominantly in manufacturing tangible personal property, for sale or profit"); *In re Erving Industries, Inc.*, 432 B.R. 354, 367-69 (2010) (finding that, for purposes of Article 2 of the Uniform Commercial Code, "electricity is tangible and *does* possess physical properties"); *see also GFI Wisconsin, Inc. v. Reedsburg Utility Comm'n*, 440 B.R. 791 (W.D. Wisc.) (electricity is a good under Article 2), *aff'g In re Grede Foundries, Inc.*, 435 B.R. 593 (Bankr. W.D. Wisc. 2010) (same). At the very least, the Court may take judicial notice that electricity is not intangible personal property and not real property. If not intangible property and not real property, electricity necessarily is tangible personal property.

The Court does not, however, need to resolve the question of whether electricity is tangible personal property. The issue is whether generating electricity is manufacturing and the Supreme Court has already held that it is. The statute at issue, section 12-6-2250, applies to entities engaged in the business of "manufacturing or any form of collecting, buying, assembling, or processing goods and materials within this State." Thus, the statute applies to entities engaged in "manufacturing." It also applies to entities engaged in "any form of collecting, buying, assembling, or processing goods and materials within this State." If either of these descriptions applies, the taxpayer must apportion its income in accordance with section 12-6-2250. Because the Supreme Court already has held that electric utilities in general and Duke Energy in particular are engaged in "manufacturing," section 12-6-2250 applies to the taxpayer in this case.

Finally, the Department must note two additional problems with Duke Energy's arguments. First, the Department's retention of an expert to testify on issues, even electricity, hardly is "an admission that material facts are in dispute," Response p.29, let alone an admission inconsistent with *Columbia Railway* and *Duke Power*. Second, Duke Energy's reference to that expert's testimony on page 29 of the response takes that testimony completely out of context. The expert did not testify that Duke Energy provides a service by manufacturing and generating electricity and distributing it to consumers, especially in the context of the metered system currently in use for measuring the electricity used by consumers. What the expert testified is that Duke Energy would be providing a service—i.e., it would be doing no more than transporting property from one point to another—***if*** the company simply provided a consumer with all the electricity they wanted for one charge. The expert explained, however, his opinion is that "if you're paying by quantity of goods transferred, then it is manufactured." [Glenn Robinson Dep. 72:12-14 [Exhibit S].]

In conclusion, the Supreme Court already has resolved the issue of whether Duke Energy falls within a taxation statute encompassing "manufacturing." Duke Energy's arguments in reply unsuccessfully attempt to evade the Supreme Court's decisions and the Department's application of those decisions. The Department therefore is entitled to summary judgment against Duke Energy on the claim that it may use the single-factor apportionment of section 12-6-2290.

3. The Department is entitled to judgment as a matter of law that Duke Energy is prohibited from including the return of principal from short-term investment transactions in the calculation of its apportionment formula.

It has been the Department's long-standing administrative policy to exclude the return of principal from short-term investment transactions in the calculation of both the "sales" factor and the "gross receipts" factor. This policy furthers the intention of the Legislature by applying an interpretation of the South Carolina allocation and apportionment provisions that considers these provisions as a whole and in light of their intended purpose while avoiding the absurdity that results from Duke Energy's interpretation of those provisions. The Court therefore should grant the Department's motion for summary judgment and deny Duke Energy's motion for summary judgment.

A. The Department has consistently interpreted the allocation and apportionment statutes and the terms "sales" and "gross receipts" as requiring the exclusion of any return of principal from short-term investment transactions.

Since at least 1977, the Department has interpreted the allocation and apportionment statutes and the terms "sales" and "gross receipts" to exclude the return of principal from short-term investment transactions. *See* S.C. Tax Comm'n Decision I-D-309, 1982 WL 176318 (June 30, 1982) [Exhibit J, Tab 7 to DOR Supp. Mem.] (stating that sales of intangible property are included in the sales factor only to the extent the sale resulted in a gain because to include the gross sales price would distort the sales factor); S.C. Tax Comm'n Decision 88-11, 1988 WL 409328 (Jan. 22, 1988) [Exhibit J, Tab 8 to DOR Supp. Mem.] (stating that it

has been the policy of the Department since 1977 to include only the gain from the sale of foreign exchange contracts in the sales factor); *see also* Br. Appellant at pp. 10-11 filed in *Duke Power* (1987) [Exhibit N to DOR Supp. Mem.] (stating that "[t]here is nothing in the record to indicate that the [Department] would consider both the principal and interest of a redeemed bond as being gross receipts" and that "the [Department] would only consider the income of the bond as gross receipts").

The Department's interpretation is entirely consistent with and furthers the purpose of the statutory allocation and apportionment framework, which is to "provide for the imposition of the South Carolina income tax, where the taxpayer is also subject to income tax in other states, 'upon a base which reasonably represents the proportion of the trade or business carried on within this State'" *See* DOR Supp. Mem. p.37 (citing *inter alia Hertz Corp. v. S. Carolina Tax Comm'n*, 246 S.C. 92, 94-95, 142 S.E.2d 445, 446 (1965) and S.C. Code Ann. § 12-6-2210). The Department's interpretation considers the language of the allocation and apportionment provisions in their entirety, including the undefined terms "sales" and "gross receipts."[28] *State v. Morgan*, 352 S.C. 359, 366, 574 S.E.2d 203, 206

[28] Although Duke Energy's Response focuses solely on the term "gross receipts" found in section 12-6-2290 (formerly section 12-7-1190, repealed in 1996) and its own strict interpretation of this term, Duke Energy acknowledges that the allocation and apportionment provisions include the term "sales" found in section 12-6-2280 (formerly section 12-7-1170). *See* Duke Energy Response pp 30-31 & n.15. As such, both of these terms must be given consideration in interpreting the allocation and apportionment provisions. If this Court affirms the Department's Determination that Duke Energy is required to file using the three-factor apportionment formula, which includes the "sales"

(Ct. App. 2002) ("Statutes must be read as a whole and sections which are part of the same general statutory scheme must be construed together and each given effect, if it can be done by any reasonable construction"); *Travelscape, LLC v. S. Carolina Dep't of Rev.*, 391 S.C. 89, 99, 705 S.E.2d 28, 33 (2011) (stating that undefined words must be construed in conjunction with the whole purpose of the statute and the policy of law).

Moreover, the Department's interpretation accurately reflects the nature of the short-term investment transactions at issue. As discussed in the Department's Supporting Memorandum, these short-term investment transactions[29] had virtually no risk, generated a minimal amount of gain or interest relative to the principal invested, and typically were outstanding for less than 30 days. [*See* Exhibit G to DOR Supp. Mem [Sherwood Love Dep. 17:4-10; 53:21-25; 58:2-7)].]. Consequently, these transactions in essence are secured loan transactions or the repeated depositing and withdrawing of money from a bank account. *See Am. Tel. & Tel. Co. v. Dir., Div. of Taxation*, 476 A.2d 800, 802 (N.J. App. Div. 1984) ("To include such receipts in the fraction would be comparable to measuring business activity by the amount of money that a taxpayer repeatedly deposited and

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factor, *see* discussion *supra* Part B, Duke Energy's entire analysis focusing solely on the term "gross receipts" would be entitled to little weight.

[29] The investment transactions included the purchase and holding to maturity of commercial paper and municipal bonds, and loan repurchase agreements ("repos"). *See* DOR Supp. Mem. p.6 (citing Love Dep. 26:15-21). Repos are overnight investment transactions typically secured by U.S. government and agency securities. *Id.* at p.6 n.8 (citing Love Dep. 26:22-27:3); *see also General Motors Corp. v. Franchise Tax Bd.*, 139 P.3d 1183, 1187 (Cal. 2006) (describing repos as "nothing more than financing arrangements by which one party provides funds to another for a short period of time").

withdrew from its own bank account. The bulk of funds flowing back to [the taxpayer] was simply its own money"); *see also General Motors,* 139 P.3d at 1192 (holding that "repo" transactions are similar to secured loans and thus, only the interest from the transaction should be included in the gross receipts factor); *Walgreen Arizona Drug Co. v. Arizona Dept. of Rev.*, 209 Ariz. 71, 77, 97 P.3d 896, 902 (Ct. App. 2004) (agreeing with comparison of return of principal from short-term investment transactions to money deposited into and withdrawn from an interest-bearing account); *Sherwin-Williams Co. v. Indiana Dept. of State Rev.*, 673 N.E.2d 849, 853 (Ind. T.C. 1996) (holding that "'gross receipts' for purposes of the sales factor includes only interest income, and not the rolled over capital or return of principal, realized for the sale of investment securities"). These transactions are wholly unlike the typical purchase-sale transactions forming the basis of the allocation and apportionment formula.

Including the return of principal from these transactions would distort Duke Energy's apportionment formula by inflating the denominator of either the "sales" or "gross receipts" factor, which in turn would unreasonably represent the business Duke Energy conducts in South Carolina. [*See* Sally Major Dep. 41:8-11 [Exhibit T] ("We interpret gross receipts in a way that will make it reasonably represent, which is what the statute says you're supposed to be doing, the amount of income that should be taxed to the state.").] Nothing in Duke Energy's Response disputes the nature of these transactions or the fact that the inclusion of the return of

principal in its apportionment formula would not reasonably represent Duke Energy's business activities in South Carolina.

The Department's policy interpreting the undefined terms "sales" and "gross receipts" prevents distortion and ensures that taxpayers' apportionment formulas result in a reasonable representation of the business conducted in South Carolina. *See Kiriakides v. United Artists Communications, Inc.*, 312 S.C. 271, 275, 440 S.E.2d 364, 366 (1994) (holding that statutes should be construed to escape absurdity and give effect to the intention of the Legislature). The Department's policy also is not "arbitrary, discriminatory or unreasonable," and thus, it is entitled to deference from the courts. *Colonial Life & Acc. Ins. Co. v. S. Carolina Tax Comm'n*, 248 S.C. 334, 339, 149 S.E.2d 777, 780 (1966) ("The Commission has the power and duty...to prescribe a method for arriving at a tax base which reasonably represents the proportion of the trade or business carried on within this State...and its determination thereabout will not be overthrown by the courts except upon a showing, absent here, that it is arbitrary, discriminatory or unreasonable") (internal quotation marks omitted); *see also Emerson Elec. Co. v. Wasson*, 287 S.C. 394, 397, 339 S.E.2d 118, 120 (1986) ("The construction of a statute by an agency charged with its administration is entitled to the most respectful consideration and should not be overruled absent compelling reasons"). The Determination therefore should be affirmed.

B. The Department has not abandoned its long-standing administrative policy.

Duke Energy cites to *Duke Power Co. v. South Carolina Tax Comm'n*, 292 S.C. 64, 354 S.E.2d 902 (1987) and South Carolina Tax Commission Decision I-D-384, 1985 WL 192739 (May 17, 1985) for the proposition that "gross receipts" should be broadly construed to include the return of principal from short-term investment transactions. Duke Energy Response pp.32-33.[30] These decisions involve whether this same taxpayer should include the proceeds from the sale of a nuclear power plant site under what is now section 12-20-100. The relevant language of the statute "levied an annual license fee of three mills upon the entire gross receipts from business within this State during the calendar year next preceding by every...Power Company." S.C. Code Ann. § 12-19-110 (1976). On its 1982 license fee return, the taxpayer reported only the proceeds from customer charges in the calculation of its license fee liability and not the proceeds from the sale of the site. The Supreme Court agreed with the Department and held that the taxpayer must include all proceeds, without subtracting costs, from the sale of the power plant.[31] Duke Energy now erroneously contends that the Department's

[30] Duke Energy also cites to Commission Decision I-D-352, 1984 WL 184988 (Mar. 26, 1984) for the same proposition, but I-D-352 relates solely to whether the damages received by a corporation for a breach of contract claim were *business* or *non-business* related for purposes of determining whether to include them in the calculation of the taxpayer's license fee liability.

[31] The Supreme Court did not directly address whether the proceeds from the sale of the power plant should be included by first subtracting the costs, but did affirm the Department's assessment in full.

interpretation in that case and subsequent Supreme Court decision support its broad construction of the term "gross receipts."

Missing from Duke Energy's discussion, though, is the fact that in the briefs submitted to the Supreme Court in *Duke Power*, both the Department AND Duke Energy stated that the return of principal from short-term investment transactions should ***not*** be included as "gross receipts." Although not at issue in *Duke Power*, Duke Energy contended that under the Department's "broad definition" of the term "gross receipts," taxpayers would have to include the receipts from the "repayment of loans" or the "liquidation of a short-term investment[,]" and that "to impose taxation in such cases ***would be absurd***." Br. of Respondent at p.15, filed in *Duke Power* [Exhibit M to DOR Supp. Mem.] (Emphasis added). Duke Energy added that an interpretation that would only impose a tax on the gain would avoid this absurdity. *Id.* at 16. The Department agreed, responding that "[t]here is nothing in the record to indicate that the [Department] would consider both the principal and interest of a redeemed bond as being gross receipts" and that "the [Department] would only consider the income of the bond as gross receipts." Br. of Appellant at p. 10-11, filed in Duke Power [Exhibit N to DOR Supp. Mem.]. Therefore, the Department has not been inconsistent in the interpretation of the term "gross receipts."

Duke Energy also cites the Supreme Court's decision in *Travelscape* interpreting the term "gross proceeds" for purposes of the sales tax. Duke Energy Response pp.31-32. But in *Travelscape*, "gross proceeds" was defined for sales tax

purposes to include "the value obtained...***without deduction for the cost of services***." *Travelscape*, 391 S.C. at 98, 705 S.E.2d at 33 (Emphasis in original). As such, the Department determined and the Court held that "[b]ecause the cost of services is ***specifically included in the definition*** of gross proceeds of sales...the fees retained by *Travelscape* for its services are taxable as gross proceeds." *Id.* (Emphasis added). Thus, in that context, the statute defined the term at issue. Here, the Department has administratively given meaning to the undefined terms "sales" and "gross receipts" in light of the statutory framework and to avoid the distortion that would result from implementing Duke Energy's theory.[32]

(3) The enactment of section 12-6-2295 in 2007 affirms the Department's long-standing administrative policy.

For over 30 years the Department has interpreted the allocation and apportionment statutes and the terms "sales" and "gross receipts" as excluding the return of principal from short-term investment transactions. Although the allocation and apportionment statutes were amended numerous times during this period, including a complete reenactment under a new chapter of the South Carolina Code of Laws in 1995, the General Assembly did not amend or alter the statutes to change the Department's policy with respect to short-term investment transactions. *See* 1995 S.C. Act 76. In light of this, the Department's policy is strongly presumed to have been approved by the General Assembly. *Ryder Truck Lines, Inc. v. S. Carolina Tax Comm'n*, 248 S.C. 148, 152-53, 149 S.E.2d 435, 437

[32] For these same reasons, references to the term "gross" outside the context of the allocation and apportionment statutes do not aid in resolving the issues in this case.

(1966); *see also Etiwan Fertilizer Co. v. South Carolina Tax Comm'n*, 217 S.C. 354, 359, 60 S.E.2d 682, 684 (1950) ("[W]here the construction of the statute has been uniform for many years in administrative practice, and has been acquiesced in by the General Assembly for a long period of time, such construction is entitled to weight, and should not be overruled without cogent reasons").

Duke Energy now contends, though, that this presumption and the General Assembly's acquiescence to the Department's policy for over 30 years should be ignored because the General Assembly now has adopted legislation ***consistent*** with the Department's long-standing policy. Although in some cases an amendment to a statute may suggest that the Legislature intended to change the law, the General Assembly may amend the law to clarify its original intent. *Stuckey v. State Budget and Control Bd.*, 339 S.C. 397, 401, 529 S.E.2d 706, 708 (2000) ("A subsequent statutory amendment may be interpreted as clarifying original legislative intent"); *see also Cotty v. Yartzeff*, 309 S.C. 259, 262 n.1, 422 S.E.2d 100, 102 n.1 (1992) ("[L]ight may be shed upon the intent of the General Assembly by reference to subsequent amendments which, although normally presumed to change existing law, may be interpreted as clarifying it."). In order for the presumption to arise that the Legislature did intend to change the law, the change would have to be "material." *See, e.g., Key Corporate, Inc. v. County of Beaufort*, 373 S.C. 55, 61, 644 S.E.2d, 675, 678 (2007) (requiring that amendment materially change the terminology of the statute in order for presumption that Legislature intended to change the law to arise). Here, the Legislature added

Section 12-6-2295 to clarify what items are "included and excluded" from the previously undefined terms "sales" and "gross receipts." S.C. Code Ann. § 12-6-2295 (2011); *see also* S. Carolina Information Letter No. 07-16, "Subject: Tax Legislative Update for 2007," 2007 WL 2702166 (Aug. 31, 2007) ("Code Section 12-6-2295 was added to provide ***examples*** of items that the terms 'sales' and 'gross receipts' do and do not include") (Emphasis added) [Exhibit U]. Notably, those definitions included the same administrative policy adopted by the Department regarding "sales" and "gross receipts." As such, there was no change in the law, let alone a material one.[33]

(4) Cases from other jurisdictions cited by Duke Energy provide no assistance in determining whether the return of principal from short-term investment transactions should be included in the calculation of Duke Energy's "sales" or "gross receipts" factors.

Duke Energy cites to cases from other jurisdictions regarding the term "gross receipts," but none of these decisions interpret South Carolina law. Each of these decisions also ignores the resulting absurdity, a crucial consideration under South Carolina law.[34] The case on which Duke Energy relies most heavily,

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[33] Section 12-6-2295 is not more limiting or restrictive than the previous law, as demonstrated by the fact that it also provides examples of items ***included*** in "sales" and "gross receipts." S.C. Code Ann. § 12-6-2295(A).

[34] In some of these cases, the courts recognized the absurdity of including the return of principal from short-term investment transactions in the calculation of the apportionment formula and sought relief from their own interpretations via other avenues. *See, e.g., Microsoft*, 139 P.3d at 1169 (using relief provision to exclude the return of principal from short-term investment transactions because including it would distort and unreasonably represent the extent of Microsoft's business in California); *Sherwin-Williams Co. v. Johnson*, 989 S.W..2d 710, 715 (Tenn. Ct. App. 1998) ("The very

Microsoft v. Franchise Tax Bd., 139 P.3d 1169 (Cal. 2006), is flawed. In *Microsoft*, the California Supreme Court held that the entire amount received when the taxpayer redeemed its securities at maturity counted as "gross receipts." *Microsoft*, 139 P.3d 1169. But that holding was based upon a concession by the state tax board:

> The Board concedes that when an investor sells a marketable security to a third party, the entire sale price is includible as gross receipts, just as it would be for the sale of any other tangible and intangible property. But from the perspective of the taxpayer, economically a sale and a redemption are indistinguishable.

Id. at 1175. In short, the tax board's concession drove the decision, a concession that does not exist in this case. In fact, on the same day, the same court held that the return of principal from loan repurchase agreements was excluded from "gross receipts." *General Motors*, 139 P.3d 1183 (holding that only the interest from loan repurchase agreements should be included in "gross receipts"). As reflected above, the Department has not taken the position reflected in the Board's concession.

The *General Motors* decision regarding repos[35] is quite pertinent. In *General Motors*, the California Supreme Court held that such transactions do not constitute "gross receipts" because these transactions were in essence secured loans. Duke Energy dismisses the *General Motors* decision because "[r]epos represent a nominal percentage of the instruments purchased and sold by Duke

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absurdity of [including the return of principal in the sales factor] lays a sound basis for the implementation of Tennessee['s alternative apportionment provision]).

[35] *See* discussion *supra* Part C.(1) & n.29 (discussing "repos").

Energy." Duke Energy Response p.43 n.17. However, based on the information that has been provided thus far,[36] it appears that the refund amount attributable to including repos would equal at least $10 million for the period from 1986 through 1998. More importantly, though, because differences in the transactions–sale of security prior to maturity, redemption of security at maturity and loan repurchase agreements–are of degree, not of kind, there is no reason to treat them differently for purposes of allocation and apportionment. Because in substance the transactions are nothing more than loans or withdrawals from interest-bearing bank accounts, including the return of principal from any of these transactions in "sales" or "gross receipts" would produce absurd results.[37]

Conclusion

For the reasons explained above and in the Supplemental Memorandum, the Department is entitled to judgment against Duke Energy as a matter of law. Because the refund claims filed by Duke Energy for periods prior to the 1994 tax year are untimely, this Court may consider only the refund claims for the periods 1994-2001. The Department is entitled to judgment as a matter of law on the remaining years because the Supreme Court has held that Duke Energy is a manufacturer of electricity and because Duke Energy is prohibited from including

[36] Duke Energy has not yet provided adequate documentation to calculate the actual amount of Duke Energy's refund claim attributable to the repos.

[37] Even if the Court grants Duke Energy's motion, the Department could require it to exclude the return of principal from the "sales" or "gross receipts" factor pursuant to section 12-6-2320 to more fairly represent Duke Energy's business in South Carolina.

the return of principal from short-term investment transactions in the calculation of its apportionment formula. Because these are all of the issues raised by Duke Energy[38] and affecting the amended returns for the Periods at Issue, this Court should grant the motion for summary judgment and dismiss this action.

Respectfully submitted,

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Attorneys for South Carolina Department of Revenue

Columbia, South Carolina
June 4, 2012

[38] Except for matters involving Crescent Resources.

EXHIBIT A

2000 WL 35525979 (S.C.Tax.Com.)

Tax Commission

State of South Carolina

SUBJECT: CLAIMS FOR REFUND AND CORRECTION OF ERRORS IN TAX YEARS BARRED BY TIME LIMITATIONS

SC **Revenue Procedural** Bulletin No. **00- 3**

December 4, 2000

EFFECTIVE DATE: Applies to all periods open under the statute.

***1 SUPERSEDES:**

SC Revenue Procedure # 95-5

Commission Decision # 93-1

All other previous documents and any oral directives in conflict herewith.

REFERENCES:

S. C. Code Section 12-60-470 (2000)

S. C. Code Section 12-60-2150 (2000)

S. C. Code Section 12-54-85 (As Amended August 2000)

S. C. Code Section 12-60-40 (2000)

AUTHORITY:

S. C. Code Ann. Section 12-4-320 (2000)

S. C. Code Ann. Section 1-23-10(4) (Supp. 1999)

SC Revenue Procedure # 99-4

SCOPE:

The purpose of a **Revenue Procedural** Bulletin is to provide **procedural** guidance to the public and Department personnel. It is a written statement issued to assist in the administration of laws and regulations by providing guidance that may be followed in order to comply with the law. **A Revenue Procedural Bulletin does not have the force or effect of law, and is not binding on the public.** It is, however, binding on agency personnel until superseded or modified by a change in statute, regulation, court decision, or advisory opinion.

INTRODUCTION

The South Carolina Code of Laws sets forth time limits within which the Department of **Revenue** must assess and collect taxes and within which taxpayers must file claims for refunds. The United States Supreme Court in Rothensies v. Electric Storage Battery Co., 329 U.S. 296 (1946) noted that the "statute of limitation is an almost indispensable element of fairness as well as of practical administration of income tax policy."

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The purpose of this advisory opinion is to set forth the Department's authority for granting refunds and briefly describe the remedies provided by law which may be available to taxpayers and the Department, where appropriate, that allow correction of errors that would otherwise be barred by time limitations.

GENERAL RULE FOR CLAIM FOR REFUND - CODE SECTIONS 12-60-470, 12-60-2150, and 12-54-85

Code Section 12-60-470 contains the general rule applicable to claims for refunds of taxes, other than property taxes. The section provides, in part:

> (A) A taxpayer may seek a refund of any state tax by filing a written claim for refund with the department. A claim for refund is timely filed if filed within the period specified in Section 12-54-85 even though the time for filing a protest under Section 12-60-450 has expired and no protest was filed.

Code Section 12-60-2150 contains the general rule applicable to claims for refunds of property taxes administered by the Department. The section provides, in part:

> (A) Subject to the time limitations in Section 12-60-1750,[1] and within the time limitation of Section 12-54-85(F), a property taxpayer may seek a refund of property taxes paid and assessed by the department by filing a claim for refund with the department if it originally assessed the property or the taxpayer believes the property is exempt, other than from the homestead exemption, from property taxes.

*2 Code Section 12-54-85, the general statutory rule for filing a claim for refund for all fees and all taxes administered and collected by the Department, provides for the time periods within which to timely file a claim for refund. The section provides, in part:

(F)(1) Except as provided in subsection (D)[2] above, claims for credit or refund must be filed within three years of the time the timely filed return, including extensions, was filed, or two years from the date of payment, whichever is later. If no return was filed, a claim for refund must be filed within two years from the date of payment.

(2) If the claim was filed by the taxpayer during the three-year period prescribed in item (1), the amount of the credit or refund may not exceed the portion of the tax paid within the period, immediately preceding the filing of the claim, equal to three years plus the period of any extension of time for filing the return.

(3) If the claim was not filed within the three-year period, the amount of the credit or refund may not exceed the portion of the tax paid during the two years immediately preceding the filing of the claim.

(4) If no claim was filed, the credit or refund may not exceed the amount which would be allowable under item (2) or (3), as the case may be, as if a claim were filed on the date the credit or refund is allowed.

SUSPENSION OF TIME LIMITATIONS FOR CLAIM FOR REFUND OR CREDIT - CODE SECTION 12-60-40

As stated above, Code Section 12-60-470 grants the Department the authority to issue refunds provided such claims are submitted within the time limitations of Code Section 12-54-85. These time limitations, however, may be extended or suspended as authorized by Code Section 12-60-40 which provides:

(A) A taxpayer may waive his rights under this chapter [Chapter 60 - The South Carolina **Revenue Procedures** Act], providing the waiver is in writing and is signed by the taxpayer or his representative. The department may extend any time limitations provided by this title and for any other taxes. The department and a taxpayer may agree to extend any time limitations or waive any requirements provided in Article 5 [State **Revenue** Appeals **Procedure**] or Article 9 [Property Tax Protest, Appeal, and Refund **Procedures**] of this chapter.

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(B) Time limitations provided under this chapter [Chapter 60 - The South Carolina **Revenue Procedures** Act] and Chapter 54 [Uniform Method of Collection and Enforcement of Taxes Levied and Assessed by the Department] are suspended during a stay ordered by the Taxpayers Rights Advocate.

See also Code Section 12-54-85(G) which provides for a suspension of the time limitations provided in subsections 12-54-85(A), (B), (C), (D), and (E) in certain situations, such as for 90 days after the date of a proposed assessment, or during the pendency of a stay ordered by the Taxpayers' Rights Advocate.

CLARIFICATION TO THE GENERAL RULE FOR CLAIM FOR REFUND

As discussed above, Code Section 12-60-470 grants the Department authority to issue a credit or refund for taxes, other than property taxes, provided such claims are submitted within the time limitations provided in Code Section 12-54-85.

***3** Consistent with its longstanding administrative position, the Department will continue to interpret the time limitations in Code Section 12-54-85 consistent with the following rules:

1. If the taxpayer agrees to the Department's request that a waiver of the time limitations on assessments be extended, then the time the Department may mail a notice of assessment pursuant to Code Section 12-54-85 will be extended. In so doing, the Department will also consider the time within which a taxpayer may file a claim for refund to be extended until the agreed upon date, however, if the Department's extension is limited in any way, such as to a particular issue, then the extension for a refund by a taxpayer will be limited in the same way. This position only applies to effective extensions agreed to in writing with the Department.

2. A taxpayer must file a claim for refund within the time limitations and state the reasons for that request. Code Section 12-60-470(B)(5) requires a claim for refund to state the amount claimed, but, if after filing a timely claim for refund, the taxpayer discovers that a refund greater than the amount originally requested is due, the Department will consider such claims, but only if the adjustment is based upon issues raised in the timely filed claim for refund. No additional refund is allowed for new issues raised after the time limitations has expired.

3. Setoff, the doctrine of equitable recoupment, or the mitigation provisions provided in Internal **Revenue** Code Sections 1311 - 1314 apply to the situation, as briefly described below.

In the Department's opinion it does **not** otherwise have the authority to allow correction of errors that are barred by the time limitations for any reason, including situations where:

1. A mistake is made calculating the expiration date of the time limitations.

2. A taxpayer failed to file a timely claim for refund when another state assessed a tax on the same income taxed in South Carolina. A taxpayer in a situation where it is undetermined which state is due the tax should file a protective claim with the Department within the time limitations. See item 2 above.

Code Section 12-60-470(G) provides that:

> Even if a taxpayer has not filed a claim for refund, if the department determines that money has been erroneously or illegally collected from a taxpayer or other person, the department, in its discretion, may, upon making a record in writing of its reasons, grant a refund to the taxpayer or other person.

Code Section 12-60-2150(G) similarly provides that:

> Even if a taxpayer has not filed a claim for refund, where no question of fact or law is involved, and it appears from the record that money has been erroneously or illegally collected from a taxpayer or other person under a mistake of fact or law, the department may, subject to the limitations in Section 12-60-1750, within the period

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specified in Section 12-54-85 and upon making a record in writing of its reasons, order a refund to the taxpayer or other person.

*4 The Department uses Code Section 12-60-470(G)[3] and 12-60-2150(G) when it audits a taxpayer and determines that the taxpayer is entitled to a refund. It has been and is the Department's longstanding administrative opinion that its right to grant a refund to a taxpayer pursuant to this section is limited by time limitations, i. e., that it cannot grant a refund unless at the time the Department grants the refund, the taxpayer could have filed a timely claim for refund. In 1995, the General Assembly enacted Code Section 12-54-85(F)(4) which is consistent with this opinion. In the opinion of the Department, if it refuses to grant a refund pursuant to this section a taxpayer is not entitled to a hearing, and the taxpayer is not entitled to appeal the Department's decision. However, if the taxpayer files a claim for refund before the expiration of the time limitation, the taxpayer is entitled to a hearing and an appeal of the Department's decision.

SUMMARY OF SETOFF, DOCTRINE OF EQUITABLE RECOUPMENT, AND MITIGATION PROVISIONS

SETOFF. In general, setoff permits all items involving the same tax and the same taxable period to be considered for adjustment in determining whether there has been an overpayment or underpayment of tax. Setoff does not permit recovery of an underpayment or overpayment in and of itself, instead it operates to decrease the recovery claimed by the other party.

Setoff may be used by the Department to reduce or eliminate a refund claimed by a taxpayer. For example, a taxpayer files a claim for refund for erroneously paid tax. Although the time limitations on assessments is closed, the Department is permitted to review the return for other errors. Setoff allows the Department to reduce the amount of the taxpayer's claim for refund by the amount of any error, the correction of which would result in additional tax being due. The refund may be reduced to zero, however, the Department may not make an additional assessment.

Setoff is also available as a remedy to taxpayers. For example, a taxpayer under audit is subject to a longer time limitation on assessments under Code Section 12-54-85(C)(1), (2), or (3). The taxpayer discovers an error, the correction of which would result in a refund, for the period under audit. Since the time limitations on claims for refund has expired, the taxpayer cannot obtain a refund. Setoff may be used by the taxpayer to setoff the potential refund amount against the amount of an assessment by the Department. The assessment may be reduced to zero, however, the taxpayer may not receive a refund.

For an interpretation of setoff by the courts see, Lewis v. Reynolds, 284 U.S. 281 (1932). The following general principles are applicable to the doctrine of setoff:

1. The claim arises from the same tax.

2. The claim arises from the same taxpayer.

3. The claim arises from the same taxable period.

THE DOCTRINE OF EQUITABLE RECOUPMENT. In general, the doctrine of equitable recoupment permits a taxpayer or a taxing authority to make up for a mistake in the tax treatment of a transaction in a closed tax period by adjusting an amount involving the same transaction in an open tax period. The doctrine, however, may only be raised in conjunction with a tax dispute that is not barred by the time limitations. Like setoff, the doctrine of equitable recoupment permits a refund claimed by a taxpayer or an assessment made by the Department to be reduced to zero, and does not permit the taxpayer to receive a refund or allow the Department to make an additional assessment.

*5 The application of the doctrine of equitable recoupment to tax law was analyzed in the following four U. S. Supreme Court decisions: Bull v. United States, 295 U.S. 247 (1935); Stone v. White, 310 U.S. 269 (1937); Rothensies v. Electric Storage Battery, 320 U.S. 296 (1946); and McEachern v. Rose, 302 U.S. 56 (1937).

Bull describes how recoupment applies to a situation involving double taxation (income tax and estate tax) of a single item of income. An estate received income from a partnership following the death of a partner. Estate tax was erroneously paid on the income. After the time limitations on filing a claim for refund for estate taxes had run, the Internal Revenue Service determined

that the partnership income was subject to federal income tax. Since the statute was open on the income tax issue, the executor paid the tax, but sued to recoup the barred overpayment of estate taxes. The court ruled that the estate should have been entitled to credit the estate tax overpayment against the income tax deficiency.

In Stone, the Internal Revenue Service used the doctrine of equitable recoupment to recoup a barred deficiency from a refund due to a related person. The trustee paid income tax on trust income. The beneficiary erroneously excluded the trust income from her individual income tax. The IRS erroneously assessed an income tax deficiency against the trust, after the time limitations was closed with respect to the beneficiary. The trustee paid the tax and sued for a refund. The Court ruled that the trustees and the sole beneficiary must be considered as one and allowed the Internal Revenue Service to recoup the deficiency of the beneficiary against the overpayment of the trust.

The following general principles are applicable to the doctrine of equitable recoupment:

1. The taxable event claimed upon and the one considered in recoupment arise from a single item or transaction occurring in different years.

2. The single transaction must be subject to two taxes based upon inconsistent legal theories.

3. The amount claimed in recoupment must be barred by the time limitations while the disputed amount must be timely.

4. If more than one taxpayer is involved, there is an identity of interest between the taxpayers.

5. It applies in situations not covered by the mitigation provisions.

THE MITIGATION PROVISIONS. The mitigation provisions are set forth in Internal Revenue Code Sections 1311 - 1314. South Carolina has adopted these Internal Revenue Code provisions, and the Department will apply them to determinations made under South Carolina income tax laws only, where applicable.

In general, the mitigation provisions permit an error to be corrected even though correction of the error in a closed year is prevented by some provision or rule of law. Unlike setoff and the doctrine of equitable recoupment, the taxpayer may receive a refund under the mitigation provisions, and the Department may make an additional assessment.

*6 Many factors must be present in order for the mitigation provisions to be used to correct an error in a year closed under the time limitations. Some of the factors include:

1. A "determination" for an open period must establish that the same item has been treated erroneously in a prior, closed year. "Determination" is defined in Internal Revenue Code Section 1313 and generally includes a court decision or administrative action.

2. On the date of the determination, the correction of the error in the closed period must be barred by the operation of law, such as the time limitations, or rule of law, such as estoppel or res judicata. Operation of law, however, does not include the mitigation provisions or offers-in-compromise.

3. The determination creates a "circumstance of adjustment" that includes one of the following conditions defined in Internal Revenue Code Section 1312:

a. Double inclusion of item of gross income,

b. Double allowance of deduction or credit,

c. Double exclusion of item of gross income,

d. Double disallowance of deduction or credit,

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e. Correlative deductions or inclusions for trusts or estates or for legatees, beneficiaries, or heirs,

f. Correlative deductions and credits for related corporations, or

g. Basis of property after erroneous treatment of prior transaction in certain circumstances.

If all of the required conditions are met, then the mitigation provisions apply and the error period is reopened for a limited period of time. The adjustment may be made to correct errors that relate to a single item or to an affected item. No other items are reopened. Internal **Revenue** Code Section 1314 sets forth the rules concerning the amount and method of adjustment.

CONCLUSION

It is the Department's policy to allow claims for refund as provided in Code Sections 12-60-470, 12-54-85, and 12-60-40, and, as provided in this advisory opinion.

Be advised that this advisory opinion is intended to provide only a brief overview of setoff, the doctrine of equitable recoupment and the mitigation provisions. There are numerous court cases and articles available that discuss these three remedies in detail. Questions concerning the specific applicability of setoff, the doctrine of equitable recoupment and the mitigation provisions should be directed to your tax advisor.

Elizabeth A. Carpentier
Director

Footnotes

1 Notwithstanding any other provision of law, Code Section 12-60-1750 provides that no refund of property taxes must be given: (1) for a property tax exemption requiring an application, unless the application was timely filed; or (2) for errors in valuation, unless the assessment was appealed in accordance with Section 12-60-2110, 12-60-2510, or 12-60-2910, as appropriate. For purposes of this item, the taxation of exempt property is not an error in valuation.

2 Notwithstanding any restrictions on filing a claim for refund provided in subsection (F), subsection (D)(3) allows a person to file a claim for refund resulting from an overpayment due to changes in taxable income made by the Internal **Revenue** Service within one hundred and eighty days after the date a final determination of tax adjustment (i.e. the federal assessment date) is made by the Internal **Revenue** Service. The refund described in this subsection applies only to the overpayment of taxes resulting from adjustments of the Internal **Revenue** Service.

3 This provision was previously contained in Code Section 12-54-30 which was repealed and replaced by Code Sections 12-60-470(G) and 12-60-2150(G) in 1995. A taxpayer was not entitled to a hearing; there was no appeal granted from an adverse decision; nor was there any reference to a statute of limitations. See Argent Lumber Co. v. Query, 178 SC 1, 182 S.E. 2d 93 (1935) where, in a similarly worded statute, the court determined that "under the terms of this act the tax commission is clothed with the power and authority to make such refunds for valid reasons, but no corresponding right is conferred upon the taxpayer to compel by suit the exercise of this authority; so that if such legislation enacted subsequent to the time of the payment of the taxes now sought to be recovered, should be held applicable, the petitioner has no legal right of redress under the specific terms of this section, for the recovery of taxes paid ...."

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EXHIBIT B

1995 WL 17817640 (S.C.Tax.Com.)

Tax Commission

State of South Carolina

SUBJECT: CLAIMS FOR REFUND AND CORRECTION OF ERRORS IN TAX YEARS BARRED BY THE STATUTE OF LIMITATIONS

SC Revenue Procedure No. 95-5 (Tax)

October 19, 1995

EFFECTIVE DATE: Applies to all periods open under the statute. Except Commission Decision # 93-1 is not superseded for claims filed prior to the amendment of Code Section 12-47-440 on June 29, 1994.

***1 SUPERSEDES:**

SC Revenue Procedure # 89-1

SC Revenue Ruling # 89-9

SC Revenue Ruling # 91-10

Commission Decision # 93-1

Commission Decision # 92-75

Commission Decision # 91-33

Commission Decision # 90-17

Commission Decision # 88-257

All other previous documents and any oral directives in conflict herewith.

REFERENCES:

S. C. Code Section 12-60-470 (1995)

S. C. Code Section 12-60-2150 (1995)

S. C. Code Section 12-54-85 (1995)

AUTHORITY:

SC Code Section 12-4-320 (Supp. 1994)

SC Revenue Procedure # 94-1

SCOPE:

A Revenue Procedure is a statement which provides information of a procedural nature. It is valid and remains in effect until superseded or modified by a change in the statute or regulations or a subsequent court decision, Revenue Procedure or Revenue Ruling.

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INTRODUCTION

The South Carolina Code of Laws sets forth time limits within which the Department of Revenue must assess and collect taxes and within which taxpayers must file claims for refunds. In some instances, the taxpayer may benefit where the Department of Revenue does not act within the required time and in other instances, the taxpayer may be disadvantaged where he does not take action within the required time.

Although the statute of limitations is arbitrary and can cause hardships, its application is designed to be neutral. As noted by the Supreme Court in Rothensies v. Electric Storage Battery Co., 329 U.S. 296 (1946), the "statute of limitation is an almost indispensable element of fairness as well as of practical administration of income tax policy."

The purpose of this document is twofold. First, this document sets forth the Department of Revenue's authority for granting refunds. Second, this document briefly describes the remedies available to taxpayers and the Department of Revenue, where appropriate, that allow correction of errors that are barred by the statute of limitations.

The principles outlined in this document are intended to replace the principles in effect under Code Section 12-47-440 (the general statutory rule for filing a claim for refund prior to the repeal of Chapter 47 in 1995), Code Section 12-54-30 (repealed in 1995), SC Revenue Procedure # 89-1, SC Revenue Ruling # 89-9, SC Revenue Ruling # 91-10, CommissionDecisions # 93-1, # 92-75, # 91-33, # 90-17, # 88-257, and all other previous documents and any oral directives in conflict herewith.

GENERAL RULE FOR CLAIM FOR REFUND - CODE SECTION 12-54-85

Code Section 12-60-470 contains the general rule applicable to claims for refunds of taxes, other than property taxes. The section provides, in part:

> *2 (A) A taxpayer may seek a refund of any state tax by filing a written claim for refund with the department. A claim for refund is timely filed if filed within the period specified in Section 12-54-85 even though the time for filing a protest under Section 12-60-450 has expired and no protest was filed.

Code Section 12-60-2150 contains the general rule applicable to claims for refunds of property taxes administered by the Department. The section provides, in part:

> (A) Subject to the time limitations in Section 12-60-1750,[1] and within the time limitation of Section 12-54-85(F), a property taxpayer may seek a refund of property taxes paid and assessed by the department by filing a claim for refund with the department if it originally assessed the property or the taxpayer believes the property is exempt, other than from the homestead exemption, from property taxes.

Code Section 12-54-85, the general statutory rule for filing a claim for refund for all fees and all taxes administered and collected by the Department of Revenue, provides for the time periods within which to timely file a claim for refund. The section provides, in part:

(F)(1) Except as provided in subsection (D)[2] above, claims for credit or refund must be filed within three years of the time the return was filed, or two years from the date of payment, whichever is later. If no return was filed, a claim for refund must be filed within two years from the date of payment.

(2) If the claim was filed by the taxpayer during the three-year period prescribed in item (1), the amount of the credit or refund may not exceed the portion of the tax paid within the period, immediately preceding the filing of the claim, equal to three years plus the period of any extension of time for filing the return.

(3) If the claim was not filed within the three-year period, the amount of the credit or refund may not exceed the portion of the tax paid during the two years immediately preceding the filing of the claim.

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(4) If no claim was filed, the credit or refund may not exceed the amount which would be allowable under items (2) or (3), as the case may be, as if a claim were filed on the date the credit or refund is allowed.

ADDITIONAL AUTHORITY FOR CLAIM FOR REFUND OR CREDIT OF TAXES OTHER THAN PROPERTY TAXES

1. CODE SECTION 12-60-40(A)

Code Section 12-60-40(A) provides for the extension of the statute of limitations and reads:

> The department and a taxpayer may agree to extend any time limitations or waive any requirements provided in Article 5 [State Revenue Appeals Procedure] or Article 9 [Property Tax Protest, Appeal, and Refund Procedure] of this chapter.

2. CODE SECTION 12-60-40(B)

Code Section 12-60-40(B) provides for time limitations to be suspensed and reads:

> Time limitations provided under this chapter [Chapter 60 - The South Carolina Revenue Procedures Act] and Chapter 54 are suspended during a stay ordered by the Taxpayers Rights Advocate.

3. CODE SECTION 12-60-470(G)

*3 In addition to Code Sections 12-54-85 and 12-60-40, Code Section 12-60-470(G) also provides for a refund or credit of taxes, other than property taxes, administered by the Department of Revenue. The statute provides that:

> Even if a taxpayer has not filed a claim for refund, if the department determines that money has been erroneously or illegally collected from a taxpayer or other person, the department, in its discretion, may, upon making a record in writing of its reasons, grant a refund to the taxpayer or other person.

This statute gives the Department the authority to grant a refund of any taxes, other than property taxes, it believes to have been paid in excess of what was due.

This provision was previously contained in Code Section 12-54-30 which was repealed in 1995. Under Code Section 12-54-30, a taxpayer was not entitled to a hearing; there was no appeal granted from an adverse decision; nor was there any reference to a statute of limitations. See ArgentLumber Co. v. Query, 178 SC 1, 182 S.E. 2d 93 (1935) where, in a similarly worded statute, the court determined that "under the terms of this act the tax commission is clothed with the power and authority to make such refunds for valid reasons, but no corresponding right is conferred upon the taxpayer to compel by suit the exercise of this authority; so that if such legislation enacted subsequent to the time of the payment of the taxes now sought to be recovered, should be held applicable, the petitioner has no legal right of redress under the specific terms of this section, for the recovery of taxes paid ...."

Therefore, a taxpayer filing a request for refund under Code Section 12-60-470(G), rather than under Code Section 12-54-85, should be aware that (1) he is not entitled to ahearing; (2) there is no appeal granted from an adverse decision; and, (3) there is no reference to a statute of limitations.

PRINCIPLES REPLACED

This revenue procedure replaces the principles set forth in SC Revenue Procedure # 89-1, SC Revenue Ruling # 89-9, SC Revenue Ruling # 91-10, CommissionDecisions # 93-1, # 92-75, # 91-33, # 90-17, # 88-257, and all other previous documents and any oral directives in conflict herewith.

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EXCEPTIONS TO GENERAL RULE FOR CLAIM FOR REFUND FOR TAXES OTHER THAN PROPERTY TAXES

Refunds will be granted in accordance with Code Section 12-54-85. For taxes, other than property taxes, the Department will allow under Code Section 12-60-470(G) correction of errors that may otherwise be barred by the statute of limitations in the following circumstances:

1. If the taxpayer agrees to the Department of Revenue's request that a waiver of the period of statute of limitations on assessments be extended, then the time the Department may mail a notice of assessment pursuant to Code Section 12-54-85 will be extended. In so doing, the time within which a taxpayer may file a claim for refund will also be extended until the agreed upon date, however, if the Department's extension is limited in any way, such as to a particular issue, then the extension for a refund by a taxpayer will be limited in the same way. This exception only applies to effective extensions agreed to in writing by the Department.

*4 2. For sales and use tax purposes, if a retailer: (1) erroneously pays sales or use tax to the person from whom he purchases property, (2) subsequently sells the property to others, (3) erroneously fails to collect sales tax and, (4) is found liable for sales tax on his sales of the property when audited by the Department of Revenue, then the retailer will be allowed to use the sales or use tax he paid to the person from whom he purchased the property as a credit against the sales tax determined to be due upon audit. This exception will allow the Department to offset the sales or use tax paid up to the amount of the assessment; it will **not** result in a refund to the retailer. In applying this exception, the retailer must: (1) provide verification that taxes were paid, and (2) obtain a written assignment of rights to a refund of sales tax from the seller from whom the property was purchased for the entire examination period.

3. A corporation must file a claim for refund with the Department of Revenue within 30 days after a final determination is received from the Internal Revenue Service. For tax years beginning after 1990, the adjustment of income by the Internal Revenue Service upon audit extends the time the taxpayer, other than a corporation, may file a claim for refund with the Department of Revenue to 180 days after the date a final determination of adjustment is received from the Internal Revenue Service. These extensions apply only when it results from an audit by the Internal Revenue Service; they do not apply to refunds of overpayments reported on the taxpayer's original return, or when the taxpayer's refund was the result of a claim for refund filed with the Internal Revenue Service. (See Code Sections 12-54-85 and 12-54-140.)

4. After filing a timely claim for refund, the taxpayer discovers that a refund greater than the amount originally requested is due. The Department will consider such claims only if the adjustment is based upon issues raised in the timely filed claim for refund. No additional refund will be allowed if a taxpayer raises new issues after the statute of limitations has expired.

5. Setoff, the doctrine of equitable recoupment, or the mitigation provisions provided in Internal Revenue Code Sections 1311 - 1314 apply to the situation, as briefly described below.

NOTE: The Department will not allow correction of errors that are otherwise barred by the statute of limitations for any other reasons including the following:

1. A mistake is made calculating the expiration date of the statute of limitations.

2. A taxpayer failed to file a timely claim for refund when another state assessed a tax on the same income taxed in South Carolina. Taxpayers in situations where it is undetermined which state is due the tax should file a protective claim with the South Carolina Department of Revenue while the statute of limitations is open. The protective claim should include the time period and issues involved, even if specific dollar amounts are not known.

SETOFF

*5 In general, setoff permits all items involving the same tax and the same taxable period to be considered for adjustment in determining whether there has been an overpayment or underpayment of tax. Setoff does not permit recovery of an underpayment or overpayment in and of itself, instead it operates to decrease the recovery claimed by the other party.

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Setoff may be used by the Department of Revenue to reduce or eliminate a refund claimed by a taxpayer. For example, a taxpayer files a claim for refund for erroneously paid tax. Although the statute of limitations on assessments is closed, the Department of Revenue is permitted to review the return for other errors. Setoff allows the Department to reduce the amount of the taxpayer's claim for refund by the amount of any error, the correction of which would result in additional tax being due. The refund may be reduced to zero, however, the Department may not make an additional assessment.

Setoff is also available as a remedy to taxpayers. For example, a taxpayer under audit is subject to a longer statute of limitations on assessments under Code Section 12-54-85(C). The taxpayer discovers an error, the correction of which would result in a refund, forthe period under audit. Since the statute of limitations on claims for refund has expired, the taxpayer cannot obtain a refund. Setoff may be used by the taxpayer to setoff the potential refund amount against the amount of an assessment by the Department. The assessment may be reduced to zero, however, the taxpayer may not receive a refund.

For an interpretation of setoff by the courts see, Lewis v. Reynolds, 284 U.S. 281 (1932).

The following general principles are applicable to the doctrine of setoff:

1. The claim arises from the same tax.

2. The claim arises from the same taxpayer.

3. The claim arises from the same taxable period.

THE DOCTRINE OF EQUITABLE RECOUPMENT

In general, the doctrine of equitable recoupment permits a taxpayer or a taxing authority to make up for a mistake in the tax treatment of a transaction in a closed tax period by adjusting an amount involving the same transaction in an open tax period. The doctrine, however, may only be raised in conjunction with a tax dispute that is not barred by the statute of limitations. Like setoff, the doctrine of equitable recoupment permits a refund claimed by a taxpayer or an assessment made by the Department to be reduced to zero, and does not permit the taxpayer to receive a refund or allow the Department to make an additional assessment.

The application of the doctrine of equitable recoupment to tax law was analyzed in the following four U. S. Supreme Court decisions: Bull v. United States, 295 U.S. 247 (1935); Stone v. White, 310 U.S. 269 (1937); Rothensies v. Electric Storage Battery, 320 U.S. 296 (1946); and McEachern v. Rose, 302 U.S. 56 (1937).

Bull describes how recoupment applies to a situation involving double taxation (income tax and estate tax) of a single item of income. An estate received income from a partnership following the death of a partner. Estate tax was erroneously paid on the income. After the statute of limitations on filing a claim for refund for estate taxes had run, the Internal Revenue Service determined that the partnership income was subject to federal income tax. Since the statute was open on the income tax issue, the executor paid the tax, but sued to recoup the barred overpayment of estate taxes. The court ruled that the estate should have been entitled to credit the estate tax overpayment against the income tax deficiency.

*6 In Stone, the Internal Revenue Service used the doctrine of equitable recoupment to recoup a barred deficiency from a refund due to a related person. The trustee paid income tax on trust income. The beneficiary erroneously excluded the trust income from her individual income tax. The IRS erroneously assessed an income tax deficiency against the trust, after the statute of limitations was closed with respect to the beneficiary. The trustee paid the tax and sued for a refund. The Court ruled that the trustees and the sole beneficiary must be considered as one and allowed the Internal Revenue Service to recoup the deficiency of the beneficiary against the overpayment of the trust.

The following general principles are applicable to the doctrine of equitable recoupment:

1. The taxable event claimed upon and the one considered in recoupment arise from a single item or transaction occurring in different years.

2. The single transaction must be subject to two taxes based upon inconsistent legal theories.

3. The amount claimed in recoupment must be barred by the statute of limitations while the disputed amount must be timely.

4. If more than one taxpayer is involved, there is an identity of interest between the taxpayers.

5. It applies in situations not covered by the mitigation provisions.

THE MITIGATION PROVISIONS

The mitigation provisions are set forth in Internal Revenue Code Sections 1311-1314. South Carolina has adopted these Internal Revenue Code provisions, and the Department will apply them to determinations made under South Carolina income tax laws only, where applicable.

In general, the mitigation provisions permit an error to be corrected even though correction of the error in a closed year is prevented by some provision or rule of law. Unlike setoff and the doctrine of equitable recoupment, the taxpayer may receive a refund under the mitigation provisions, and the Department may make an additional assessment.

Many factors must be present in order for the mitigation provisions to be used to correct an error in a year closed under the statute of limitations. Some of the factors include:

1. A "determination" for an open period must establish that the same item has been treated erroneously in a prior, closed year. "Determination" is defined in Internal Revenue Code Section 1313 and generally includes a court decision or administrative action.

2. On the date of the determination, the correction of the error in the closed period must be barred by the operation of law, such as the statute of limitations, or rule of law, such as estoppel or res judicata. Operation of law, however, does not include the mitigation provisions or offers-in-compromise.

3. The determination creates a "circumstance of adjustment" that includes one of the following conditions defined in Internal Revenue Code Section 1312:

a. Double inclusion of item of gross income,

*7 b. Double allowance of deduction or credit,

c. Double exclusion of item of gross income,

d. Double disallowance of deduction or credit,

e. Correlative deductions or inclusions for trusts or estates or for legatees, beneficiaries, or heirs,

f. Correlative deductions and credits for related corporations, or

g. Basis of property after erroneous treatment of prior transaction in certain circumstances.

If all of the required conditions are met, then the mitigation provisions apply and the error period is reopened for a limited period of time. The adjustment may be made to correct errors that relate to a single item or to an affected item. No other items are reopened. Internal Revenue Code Section 1314 sets forth the rules concerning the amount and method of adjustment.

CONCLUSION

It is the Department's policy to allow claims for refund as provided in Code Sections 12-54-85, 12-60-40, and 12-60-470(G), as provided in this document.

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Be advised that this revenue procedure is intended to provide only a brief overview of setoff, the doctrine of equitable recoupment and the mitigation provisions. There are numerous court cases and articles available that discuss these three remedies in detail. Questions concerning the specific applicability of setoff, the doctrine of equitable recoupment and the mitigation provisions should be directed to your tax advisor.

Burnet R. Maybank, III
Director

Footnotes

1 Notwithstanding any other provision of law, Code Section 12-60-1750 provides that no refund of property taxes must be given: (1) for a property tax exemption requiring an application, unless the application was timely filed; or (2) for errors in valuation, unless the assessment was appealed in accordance with Section 12-60-2110, 12-60-2510, or 12-60-2910, as appropriate. For purposes of this item, the taxation of exempt property is not an error in valuation.

2 Notwithstanding any restrictions on filing a claim for refund provided in subsection (F), subsection (D) allows a corporation to file a claim for refund resulting from an overpayment due to changes in taxable income made by the Internal Revenue Service within thirty days from the date the Internal Revenue Service changes the taxable income.

End of Document

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EXHIBIT C

STATE OF SOUTH CAROLINA
ADMINISTRATIVE LAW COURT

Duke Energy Corporation, Petitioner, vs. South Carolina Department of Revenue, Respondent,	)	Docket No. 10-ALJ-17-0270-CC

Affidavit of Ronald W. Urban

1. I am over eighteen (18) years of age and of sound mind and qualified to give this affidavit.

2. I have a J.D. from the University of South Carolina School of Law.

3. I am a member of the South Carolina Bar.

4. From 1980 to 1995, I was employed by the South Carolina Attorney General's Office and assigned to work with the South Carolina Tax Commission, first as an Assistant Attorney General and later as a Deputy Attorney General.

5. My office was located at the Tax Commission, and I had daily contact with the Commissioners.

6. My responsibilities included advising the Tax Commission with respect to many areas of tax policy and law.

7. My duties included issuing Attorney General's Opinions to the Commissioners on behalf of the Attorney General regarding various tax matters.

8. I attended hundreds of Tax Commission hearings and assisted the Commissioners in the decision making process.

9. I drafted the findings and conclusions of law on behalf of the Commissioners for their review and signature in hundreds of cases.

10. Once the Commission issued a decision, I represented it in all subsequent litigation concerning that decision.

11. In 1995, the Department of Revenue was created and I transferred to the General Counsel's Office for the Department.

12. I worked with the Department of Revenue from 1995 until 2010.

13. During 1995 until 20120, I served as Chief Counsel for Revenue Litigation; Chief Counsel for Litigation; and General Counsel for Litigation for the Department.

14. In those roles, I provided legal advice to the Director of the Department of Revenue and to Department employees.

15. I also managed litigation cases as well as litigating cases for the Department.

16. I have reviewed the affidavits submitted in this matter by Marvin Davant and Robbie Anderson.

17. Although I worked with the Tax Commission and the Department for 30 years, the first time I recall having seen a Form FS-43 was when one was shown to me prior to my deposition in this case.

18. To the best of my knowledge, the Tax Commission never approved Form FS-43 or adjudicated a case where Form FS-43 was at issue.

19. Based on the "FS" designation, Form FS-43 appears to be a document prepared by Field Services for its own use with respect to examinations.

20. To the best of my knowledge, Form FS-43 was never approved as an official form by the Department.

21. This conclusion is supported by Mr. Davant's assertion that the form had been in use for many years, because prior to the 1980s, the Tax Commission was divided into divisions based on the different taxes collected by statute and there was little centralized management of issues such as standardized forms prior to the 1980s.

22. Although Mr. Davant and Mr. Anderson state that it was their understanding that Form FS-43 would extend the time for the Department to assess taxes as well as the time in which the taxpayer could file a refund claim, that it is not my understanding of the pertinent statutes or of Tax Commission policy prior to 1995.

23. It is my recollection that the Tax Commission consistently took the position that the time limitations set forth in refund statutes could not be extended or altered prior to 1995.

24. As a review of various policy documents from the years prior to 1995 indicate, the Tax Commission initially believed that the refund provisions of South Carolina Code Section 12-47-440 applies to all taxes.

25. In 1990, the South Carolina Supreme Court held in the Bass decision that section 12-47-440 did not apply to income taxes and that the taxpayer's sole remedy was to proceed under section 12-47-220.

26. The General Assembly later amended section 12-47-440 to apply to income taxes, but only for the years 1990 and later.

27. Therefore, prior to 1990, the taxpayer's remedy for obtaining a refund was to proceed under section 12-47-220 and pay taxes under protest, then institute an action in circuit court within 30 days.

28. For the years 1990-1994, a taxpayer could claim a refund under section 12-47-440 within three years of the date the payment was due, without regard to any extensions.

29. To the best of my recollection, the view of the Tax Commission was that refund limitations periods could not be extended because there was no authority for any such extensions prior to 1995.

30. To the best of my recollection, the basis for this view was that case law states refund statutes are strictly construed; that the statutes contained

no provision for extensions of time; and that the General Assembly would have provided for extensions of time if it wanted to make that remedy available (which it did in 1995).

31. That this was the Tax Commission's position is shown by Technical Advice Memorandum 89-3, which is attached to this affidavit as Exhibit A.

32. The interpretation advanced by Mr. Davant and Mr. Anderson is completely inconsistent with this statutory framework for refund periods, which was consistently applied by the Tax Commission.

33. Therefore, as applied to years before 1995, Form FS-43 appears to extend the time for assessments only, which is the authority granted by the statute it references: section 12-54-80.

34. In my opinion, the reference to refunds in Form FS-43 references the remedy available under section 12-54-30 (previously 12-7-2240), which provided that if a refund situation was identified as part of an examination, the Tax Commission would grant that refund.

35. However, there was no right of appeal from any decision under section 12-54-30.

[SIGNATURE AND NOTARIZTION PAGE FOLLOWS]

This 4 day of June, 2012.

Ronald W. Urban

Sworn to and subscribed before me,
this 4 day of June 2012

Notary Public for the State of South Carolina
My Commission expires: 2/11/2018

EXHIBIT D

STATE OF SOUTH CAROLINA
ADMINISTRATIVE LAW COURT

DUKE ENERGY CORPORATION,

Petitioner,

vs. DOCKET NO. 10-ALJ-17-0270-CC

SOUTH CAROLINA DEPARTMENT OF REVENUE,

Respondent.

D E P O S I T I O N

WITNESS: T. COOPER MONROE, III

DATE: December 5, 2011

TIME: 10:19 a.m.

LOCATION: Law Offices of
Nexsen Pruet
227 West Trade Street
Charlotte, North Carolina

TAKEN BY: Attorneys for the Defendants

REPORTED BY: Carolyn M. Beam
Court Reporter

COMPUSCRIPTS, INC.
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Q. And that document request waivers so that -- so that we can finish this audit once the IRS audit is finalized. Is that what it says? And that would be the page marked 302 of Exhibit 10.

A. Did you say once the audit is finalized?

Q. I believe it says once the audit is finalized.

A. Okay. Yes.

Q. And then there is one on the next page dated a little bit earlier than that, I think 3/3/89, and asked about finalizing the audit, correct?

A. It didn't appear to be asking about finalizing the audit.

Q. Okay. Tell me what it means to you.

A. Well, it just says so that they can finalize the audit.

Q. Okay. So during much of the 1980s there was an IRS audit going on regarding Duke Energy?

A. Correct.

Q. And then attached to that are just two of the waiver forms we've already looked at, I think. All right. I want to you to tab -- excuse

me, Exhibit 11. That also is a document from Randy Wilson to Remi Taylor, right?

A. Yes.

Q. And the language there is very similar to the one we looked at on Exhibit 10, correct?

A. Correct.

Q. And now the response at the bottom is different though, correct?

A. Correct.

Q. And it says, our case is still in appeals. I'll let you know when we settle. Is that correct?

A. Correct.

Q. Do you know what the appeal was from? In other words, what was on appeals regarding the -- I assume, the IRS audit, do you know?

A. What years or what issues?

Q. What issues.

A. I think there was a host of issues. One large one had to do with how gains from the sale of the undivided interest in Catawba nuclear station was characterized for federal purposes, the capital, short-term, long-term versus ordinary.

Q. Was that the primary issue?

A. I believe it was the largest --

Q. Largest.

A. -- dollar amount issue.

Q. That's what I mean by primary. Okay. Was it beneficial to Duke to delay any South Carolina audits until the IRS audit process was completed?

A. It would have the benefit of only having to audit the years once for South Carolina instead of multiple times.

Q. And that would save you resources in dealing with the audit -- you, being Duke Energy -- in dealing with the audit, correct?

A. Potentially.

Q. Is it -- is it -- strike that.

Is it time consuming, from the, I guess, employee standpoint, to deal with tax audits? Do the employees have to spend a lot of time providing information, compiling information and the like to respond to auditor requests for information or documents?

A. It takes a certain amount of time, yes.

Q. I think Mr. McCarver's affidavit indicated that, paragraph six, every year during the period at issue, South Carolina auditors would travel to and spend a week at the offices of Duke

Energy reviewing documentation relating to the income tax audit for that particular year. Does -- what happens when auditors show up at Duke Energy's office to perform an audit? Do you put them in an office? Do you give them office space?

A. Yes, we give them office space.

Q. Do you assign employees to deal with their information needs and documents and things like that?

A. Yes.

Q. And does it take those employees away from other duties that they might be performing for the company?

A. Currently, I have a full-time state tax audit manager whose vast majority of his duties are to respond to state auditors. To the extent he schedules them efficiently -- you know, I guess there might be a time when states quit auditing us. I doubt that. But, yeah, potentially he could be doing something else, so yes.

MR. GREEN: Tab 17.

(DFT. EXH. 12, Letter dated March 8, 1991 and handwritten memo dated 3/11/91, Bates StampSCDOR00003767 and 3768, marked for identification.)

Wilson from Burnet Maybank. And it looks like Bernie's -- and it says: I know that you have had a very rough year and have much bigger fish to fry at the current time than finishing the audit report, so we would very much appreciate your providing us with another extension. I will be knocking off for vacation next Tuesday so, for selfish reasons, I would appreciate you providing us with an extension in the next few days. And then it discusses the license tax and extension.

So, in that instance, it looks like Bernie is sort of requesting an extension of time, correct?

A. He is requesting an extension.

MR. GREEN: Duke 20. Tab 20.

(DFT. EXH. 15, Letter dated December 16, 1999, Bates Stamp DES00000329, marked for identification.)

BY MR. GREEN:

Q. Let me know when you've had a chance to read it. Have you ever seen this document before?

A. Doesn't look familiar.

Q. Okay. You had mentioned earlier, I think, a reference to Remi Taylor. I'm not sure I jotted it in my statements. Isn't a reference to

it here. Anyway, this indicates that Remi Taylor, principal tax manager, was signing waivers annually, as he said, that it would be easier to settle all issues when IRS audit finished the appeals process, et cetera. Do you know if that was Duke Energy's position at the time the waivers were being signed and the IRS audit was ongoing?

A. From the record, that's the way it appears.

MR. GREEN: Okay. Tell you what, let's take a little break, if we could.

(A recess transpired.)

(DFT. EXH. 16, Handwritten document headed Duke, marked for identification.)

BY MR. GREEN:

Q. Have you seen this document before?

A. Yes.

Q. Correct me if I'm wrong, but I think you referenced earlier a document regarding a verbal understanding by Remi Taylor. Is this the document you're referring to?

A. Yes.

Q. And if I -- the letter appears to represent, in accordance with a verbal agreement, that I will notify you when we have settled year

you back to those forms for a minute, and I don't have the exhibit numbers here, I'm sorry, but it's form 872. And the first waiver, which was executed on August 16, 1988.

A. So 872 is Exhibit 8.

Q. And the waiver executed on 8/16/88 is Exhibit 7. If I can direct your line -- your attention, first, to form 872, middle of the page, number two. That says the taxpayer may file a claim for a credit or a refund. And the service may credit or refund the tax within six months after this agreement ends, correct?

A. Correct.

Q. And does the South Carolina form also mention the ability of the taxpayer to file a refund claim?

A. Yes.

Q. Okay. Thank you. Mr. Green also referenced -- asked you a few questions about whether it would take time or extra resources for Duke if South Carolina Department of Revenue had audit -- to go through two audits. When a South Carolina auditor comes on site, typically, are they generally working on other matters or are they generally focussed on the -- the Duke audit while

they're sitting at your facility?

A. While they're sitting at our facility, they're concentrating on Duke matters.

Q. So that auditor, if he was on site for a week, as I think was referenced in one of the prior letters, you -- that auditor would be tied up for the full week and that would take his attention 100 percent away from other matters, correct?

A. Yes.

Q. And you mentioned that Duke employs individuals in their tax department that are responsible for dealing with federal and state tax audits, correct?

A. Correct.

Q. And if the South Carolina auditor were on site, would that person be required to spend 100 percent of their time on the South Carolina audit for the week that the South Carolina auditor was on site?

A. Most likely.

Q. Okay. With regard to the settlement questions we just spoke about, what's your understanding of the difference between an 870, a South Carolina form 870 and a South Carolina form 870 AD?

EXHIBIT E

DUKE POWER COMPANY
TAX DEPARTMENT
422 SOUTH CHURCH STREET
CHARLOTTE, N. C. 28242-0001

JOHN P. O'KEEFE
VICE PRESIDENT TAXES
(704) 373-6231
WILSON R. TAYLOR
MANAGER, INCOME TAXES
(704) 373-4206
JOE L. WALLACE
MANAGER, PROPERTY TAXES
(704) 373-4203

RICKEY A. McCARVER
(704) 373-5706
H. LYNN BOYETTE
(704) 373-2781
LARRY C. AUTEN
(704) 373-8376
RICHARD L. ROGERS, JR.
(704) 373-3213
TELECOPIER:
(704) 373-6994

April 19, 1991

Mr. Harold Ingram
Field Services Division
South Carolina Tax Commission
P. O. Box 125
Columbia, SC 29214

Dear Mr. Ingram:

In accordance with our verbal agreement that I would notify you when we had settled years 1978-1983 with the IRS, we received notification on March 12, 1991 that these years had been accepted by the Joint Committee. We have filed a protest for 1984 and 1985 on some issues.

Very truly yours,

Remi Taylor

RT/cj



EXHIBIT F

DUKE POWER COMPANY

TAX DEPARTMENT
422 SOUTH CHURCH STREET
CHARLOTTE, N. C. 28242-0001

JOHN P. O'KEEFE
VICE PRESIDENT, TAXES
(704) 373-6231

WILSON R. TAYLOR
MANAGER, INCOME TAXES
(704) 373-4208

JOE L. WALLACE
MANAGER, PROPERTY TAXES
(704) 373-4803

RICKEY A. McCARVER
(704) 373-6166

H. LYNN BOYETTE
(704) 373-2781

LARRY C. AUTEN
(704) 373-6316

RICHARD L. ROGERS, JR.
(704) 373-6272

[illegible]
(704) 373-6884

March 8, 1991

Mr. John Swearingen
South Carolina Tax Commission
P.O. Box 125
Columbia, SC 29214

Re: Duke Power Company
E.I.N. 56-0205520
1989 SC Form 1120U

Dear John:

Thank you for your call informing us that we had made an error on the calculation of our Palmetto Seed Capital Credit in 1989 in the amount of $135,000 and that our account as corrected shows an overpayment of such amount.

We request that you take the necessary action to issue us a cash refund of the overpayment.

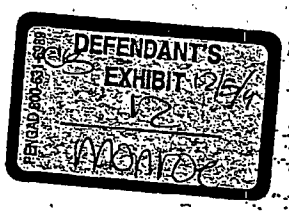
Again, thank you for bringing this error to our attention.

Very truly yours,

Rickey A. McCarver

Rickey A. McCarver

RAM/cj



SCDOR00083767

3/11/91

Memo

To: Corporate Section

From: John Swanger

Re: DUKE POWER - 1989 SC 1120A
FILE # 2029004
CBL # 1405 2115
Overpayment $135,000

Upon review of the 1989 return of Duke power, it is apparent Duke understated its credit for investment in the Palmetto Seed Capital Corporation. Duke multiplied $1,000,000 by .30 and got $30,000 rather than $300,000 and on line 7 multiplied $500,000 by .30 and got ~~$150,000~~ $150,000 instead of $150,000. Since line 7 was the smaller amount Duke limited the 1989 credit to $15,000 instead of $150,000. Duke is due or refund of ~~$150,000~~ $135,000.

Attached is a request from Rick McCraven requesting the refund - ~~His~~ Her number is (704) 373-5706 if you need more info.

SCDOR00003768

EXHIBIT G

Duke

Waiver - 1996 (Nov) - Joe Sr. + I started work on 78 → RAR + the returns ~~(78, 84, 85)~~

Remi Taylor, the prior tax manager, was signing waivers annually as he said that it would be easier to settle all issues when IRS audit finished the appeals process, etc.

In Nov, 1994 Joe + I went in to do audit. I think '83 forward had waivers signed. This is when we received 78 → 85 RARs. I have notes where we were picking up '83 interchange revenues for license fee ('84) so 83 was still open

SCDQR00009154

EXHIBIT H

NEXSEN PRUET JACOBS POLLARD & ROBINSON, LLP
ATTORNEYS AND COUNSELORS AT LAW

Burnet R. Maybank
SPECIAL COUNSEL

DIRECT DIAL
(843)
720-1768
BRM@NPJP.
COM

December 16, 1999

VIA FACSIMILE
Mr. Randy Wilson
Department of Revenue
PO Box 125
Columbia, SC 29214

RE: Duke Energy Audit

Dear Randy:

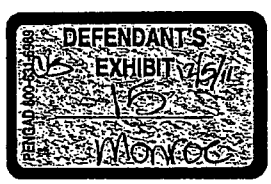
I am very pleased to report that I am assisting the various Duke Power entities on a variety of tax issues. (For a young felloe building a law practice, Duke Power is a good place to start!)

The Tax Department in Charlotte has asked me to help with the Duke Energy income and license tax audits for the years 1978-1993. It is my understanding that the extensions on all of these returns will expire on December 31, 1999. I know that you have had a very rough year and have much bigger fish to fry at the current time than finishing the audit report, so we would very much appreciate your providing us with another extension. I will be knocking off for vacation next Tuesday, so for selfish reasons, I would appreciate your providing us with an extension in the next few days. I understand Joe Southard is handling the license tax issue. Could you also grant us an extension in this regard?

I hope things take a turn for the better for you and will contact you probably in February to discuss the audits.

Yours very truly,

Burnet R. Maybank



BRM\mwj

NPCHAR1:127507.1-LT-(BRM) 800000-00181

EXHIBIT I

DUKE POWER COMPANY
TAX DEPARTMENT
POST OFFICE BOX 33189
CHARLOTTE, N. C. 28242

JOHN R. O'KEEFE
VICE PRESIDENT, TAXES

(704) 373-6231

December 27, 1988

Mr. Randy Wilson
South Carolina Tax Commission
P. O. Box 125
Columbia, SC 29214

Dear Mr. Wilson:

We have not received the consent to extend the time for assessment of income tax and license for 83/84 and 84/85 respectively. Enclosed is a signed copy of the previous consent that has been modified to extend the date to March 31, 1989.

Very truly yours,

John P. O'Keefe

JPO/cj

Enclosure

DES00000305

SOUTH CAROLINA TAX COMMISSION
FIELD SERVICES DIVISION
CONSENT TO EXTEND THE TIME TO ASSESS TAX

File No. 20090024-9

Duke Power Company — SSN
Name of Taxpayer(s)

Po Box 33189 Charlotte NC 28242
Address (Number, Street, City or Town, State, Zip Code)

and the SOUTH CAROLINA TAX COMMISSION consent and agree to the following:

(1) The amount of any STATE Income Tax / License Fee tax due on any return(s) made by or for the above taxpayer(s) for the period(s) ended December 31, 1983/84 and December 31, 1984/85

may be assessed at any time on or before March 31, 1989
(Expiration Date)

This agreement extends the time for mailing the notice of assessment or refund of the above tax pursuant to the provisions of Section 12-54-80 of the 1976 South Carolina Code of Laws, as amended.

Duke Power Company
(Name of Taxpayer)

By: John F. O'Kelley
(Taxpayer, Partner, Officer of Corp., etc.)

Vice President, Taxes
(Title)

December 27, 1988
(Date)

SOUTH CAROLINA TAX COMMISSION

By: _____
(Director, Field Services Division)

_____
(Date)

If this waiver is executed on behalf of a corporation, it will be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition, to which the seal, if any, of the corporation must be affixed.

FS-43 (11/85)

DES00000306

EXHIBIT J

STATE OF SOUTH CAROLINA

ADMINISTRATIVE LAW COURT

DUKE ENERGY CORPORATION,

Petitioner(s),

vs. Case No: 10-ALJ-17-0270-CC

SOUTH CAROLINA DEPARTMENT OF REVENUE,

Respondent(s).

D E P O S I T I O N

WITNESS: JAN URBAN

DATE: Wednesday, December 21, 2011

TIME: 10:33 a.m.

LOCATION: Willoughby & Hoefer, P.A.
930 Richland Street
Columbia, South Carolina

TAKEN BY: Attorneys for the Petitioner

REPORTED BY: SHERI L. BYERS
Registered Professional Reporter

- -

COMPUSCRIPTS, INC.
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1-888-988-0086
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APPEARANCES:

ATTORNEYS FOR THE PETITIONER
DUKE ENERGY CORPORATION:

SUTHERLAND ASBILL & BRENNAN
BY: ERIC S. TRESH, ESQUIRE
-and- MARIA M. TODOROVA, ESQUIRE
999 Peachtree Street NE
Atlanta, Georgia 30309
eric.tresh@sutherland.com
maria.todorova@sutherland.com
404.853.8214

NEXSEN PRUET, LLC
BY: RICK REAMES III, ESQUIRE
1320 Main Street, 7th Floor
Columbia, South Carolina 29201
rreames@nexsenpruet.com
803.540.2048

ATTORNEYS FOR THE RESPONDENT
SOUTH CAROLINA DEPARTMENT OF REVENUE:

WILLOUGHBY & HOEFER, P.A.
BY: TRACEY C. GREEN, ESQUIRE
-and- JOHN W. ROBERTS, ESQUIRE
930 Richland Street
Columbia, South Carolina 29201
tgreen@willoughbyhoefer.com
jroberts@willoughbyhoefer.com
803.252.3300

ALSO PRESENT:

T. COOPER MONROE, III, MANAGING DIRECTOR
J. ABRAHAM GUTTING, COUNSEL FOR LITIGATION

(INDEX AT REAR OF TRANSCRIPT)

back, correct?

A. Correct.

Q. Okay. And to your knowledge, did the Department ever send a similar 870AD for income taxes?

A. Based on the chain of correspondence, it doesn't appear that we would have sent an AD for income taxes.

Q. Is there any reason why you would send one for sales taxes and not for income taxes?

A. It wouldn't -- Duke was requesting an SC870, not an SC870AD. And we -- this was executed in August. The chain of correspondence in which they made clear that they did not want to execute an 870AD was prior to that time, so we apparently did not send them one.

Q. Are you aware of any other document or agreement signed by the Department and Duke Energy that would have prohibited Duke from filing refund claims, in other words, that would have settled their income -- would have prohibited them from filing income tax refund claims? Is there any written settlement agreement between Duke Energy and the Department that you're aware of?

A. I'm not aware of any other written settlement agreement other than the document that you provided that was signed by Mr. Swearingen.

Q. And that document would have held open the periods for Duke to file refunds; is that correct?

A. Would have held open certain periods.

Q. Otherwise open periods?

A. Exactly.

MR. TRESH: Okay. Let's look at 21782.

(PETITIONER'S EXH. 11, Letter Dated December 19, 2002, SCDOR00021782, was marked for identification.)

BY MR. TRESH:

Q. Okay. This is a letter from John Comer to Duke Energy dated December 19, 2002. Do you agree?

A. Correct.

Q. And Mr. Comer was an audit manager for the South Carolina Department of Revenue; is that correct?

A. Yes, sir.

Q. And have you seen this letter before?

A. I don't recall seeing that, no, sir.

Q. Okay. Can you take a moment to look over the letter?

A. Certainly.

Q. Would you agree that this letter was a letter to Mr. Priesmeyer, who was at Duke Energy at the time, and it closed the sales and use tax audit for Duke Energy?

A. Correct.

years open for both the DOR and the state until the end of the waiver period, 12-31-2002."

A. Yeah. I'm sorry.

Q. Is that correct?

A. That's correct. What I cannot address is what those years were.

Q. Okay.

A. That's simply the clarification I'm attempting to make.

Q. Based upon your recollection having been directly involved in this process, do you have any reason to -- do you have any reason to believe that the years at issue in that letter that Mr. Swearingen was executing and agreeing to hold open were not '78 through 2001, is there anything you can recall that would indicate otherwise?

A. From this chain of e-mails, there's an indication that they were looking for credits and adjustments and my -- I don't have a direct strong recollection. I would -- I would -- it indicates to me that they were looking at later years and I --

Q. When you say "later years," what do you mean by that?

A. Years -- and I'm not sure what year South Carolina adopted. We started -- the legislature

adopted additional tax credit incentives recruiting industry and recruiting investment in South Carolina. And I'm not exactly sure what those later years were, but it was not as far -- there were many more incentives in the later years than there were in the early '70s.

Q. So for the period '78 through 2001, that is the subject of this e-mail chain, are you suggesting that Duke wanted to file refund claims or that these credits or incentives related to years after 2001, before 2001? What was Duke asking to hold the statute open for?

A. I'm not sure of the answer to what years they were asking, but my thought would be from my e-mail that they were gathering information about credits for more recent years. That it wasn't for this very long period.

Q. If it was for more recent years, why would they have needed some sort of agreement to hold the statute of limitations open? In other words, if it was for years that were within the statute, why would they need anything?

A. Years that were covered by the audit.

Q. Oh, okay. So years --

A. But not the -- more recent. The audit covered, as you know, a large number of years. I'm thinking that this related to the more recent years in

the audit period. Not years subsequent to the audit.

Q. Is there anything in this e-mail correspondence or any correspondence that you're aware of that would in some way limit where Duke was suggesting that they only hold open part of the statute of limitations?

A. Yeah.

Q. What part would that be?

A. In your Exhibit 21661, Mr. Priesmeyer is writing to me, "Duke is planning on filing amended returns for some credits and other deductions/ adjustments not previously taken for these years."

I'm thinking that those are credits for more recent years that they're assembling information for. It doesn't state that. It's not clear.

Q. Is it true you stated earlier that these e-mails refer to the period '78 through 2001; is that correct?

A. Correct.

Q. So when Mr. Priesmeyer's e-mail when he says, "these years," do you have any reason to believe that he was referring to anything other than '78 through 2001?

A. Yeah. It's not my belief that they were going back in the records to '78 to pull out property that would qualify for investment tax credits. I just

Q. And that document would have held open the periods for Duke to file refunds; is that correct?

A. Would have held open certain periods.

Q. Otherwise open periods?

A. Exactly.

MR. TRESH: Okay. Let's look at 21782.

(PETITIONER'S EXH. 11, Letter Dated December 19, 2002, SCDOR00021782, was marked for identification.)

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Q. Okay. This is a letter from John Comer to Duke Energy dated December 19, 2002. Do you agree?

A. Correct.

Q. And Mr. Comer was an audit manager for the South Carolina Department of Revenue; is that correct?

A. Yes, sir.

Q. And have you seen this letter before?

A. I don't recall seeing that, no, sir.

Q. Okay. Can you take a moment to look over the letter?

A. Certainly.

Q. Would you agree that this letter was a letter to Mr. Priesmeyer, who was at Duke Energy at the time, and it closed the sales and use tax audit for Duke Energy?

A. Correct.

EXHIBIT K

NEXSEN PRUET JACOBS & POLLARD, LLC
ATTORNEYS AND COUNSELORS AT LAW

BURNET R. MAYBANK III
MEMBER

DIRECT DIAL
803-253-8228
BMaybank@NPJP.com

July 2, 2002

Mr. John A. Swearingen
Audit Supervisor
Department of Revenue
301 Gervais Street
Columbia, South Carolina 29201

Jan Steensen Crangle, CPA
Manager, Office of Appeals
South Carolina Department of Revenue
Post Office Box 125
Columbia, South Carolina 29214

Re: Proposed Duke Settlement

Dear John and Jan:

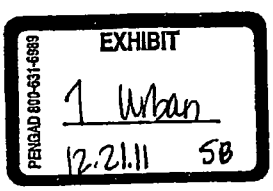
Duke offers the following settlement proposal:

SALES TAX

Duke would like to settle the sales tax liability though 2001, using the methodology and quarterly tax liability contained in your fax. (See attached Exhibit 1.) This includes accepting the DOR's interest rate calculation. Duke proposes to execute a SC870AD regarding the sales and use tax liability through 2001. We understand this equals approximately ($2,796,623) with interest calculated through April 5, 2002.

INCOME AND LICENSE TAXES

Duke proposes accepting the DOR's proposal except that it would agree to execute a SC870, rather than a SC870AD. We understand this would have the effect of keeping the years open for both the DOR and the State until the end of the waiver period (12/31/2002), unless the DOR and Duke jointly agree to execute another waiver. As previously indicated, Duke is examining the possibility of filing amended returns.



SCDOR00021667

We understand that this equals a refund of $5,891,208 (with interest calculated through July 2, 2002.)

We would also like to accept your proposal that the DOR would issue a FAD (at our request) on the calculation of interest on the income and license taxes so that we could contest the interest rate calculations. (Duke may not contest the matter, but we would like to retain the option.)

CONCLUSION

We have pretty well agreed to all of the DOR proposals, so I trust you find this satisfactory. Duke would like to have the attached schedule (Exhibit 2) re-calculated with interest brought forward to no later than July 15th. Additionally, Duke would like for all these matters to be combined for settlement purposes and the DOR issue a refund in a timely manner for the net amount.

If the attached accurately reflects your understanding, please execute a copy of this letter and return it to us. We look forward to receiving the 870 and the 870AD which we will execute and return to you.

With kind regards, I am

Yours very truly,

Burnet R. Maybank III

BRM/kc
cc: Mr. Harley Priesmeyer/Duke Energy

John Swearingen
DOR

July 8, 2002

SCDOR00021668

EXHIBIT L

From: "Harley H Priesmeyer" <hhpriesmeyer@duke-energy.com>
To: <crangl@sctax.org>
Date: 7/10/02 4:16PM
Subject: Form SC870

Jan - alternatively, we could do without the SC870 for income/license fee if you guys are agreeable to pay us the net amount of approximately $3 million and we get a FAD for the interest calculation. If you are in agreement with this arrangement, let me know and we'll revise the settlement letter.

Harley Priesmeyer
Director, State and Local Taxes
Duke Energy Corporation
P. O. Box 1642
Houston, Texas 77251-1642

Office: 713-989-3285
Fax: 713-989-3280
Cell: 713-501-0725
email: hhpriesmeyer@duke-energy.com

---- Forwarded by Harley H Priesmeyer/Tax/PSC/PEC on 07/10/2002 12:04 PM ----

Harley H Priesmeyer
07/10/2002 11:06 AM

To: crangl@sctax.org
cc: bmaybank@npjp.com
Subject: Form SC870

Jan - I received your voice mail re why we needed to do a SC870 instead of a SCAD870 form. There are two reasons for it. One, Duke wants to reserve the right to contest the interest computation on the income/license fee and secondly, Duke is planning on filing amended returns for some credits and other deductions/adjustments that were previously not taken for these years.

Hopefully, this will aid you re this matter. I remember seeing some previous correspondence from Burney in which you were ok with Duke signing an 870 form.

If you need anything else on this, please let me know.

Harley Priesmeyer
Director, State and Local Taxes
Duke Energy Corporation
P. O. Box 1642
Houston, Texas 77251-1642

EXHIBIT M

From: JAN CRANGLE
To: Priesmeyer, Harley H
Date: 7/10/02 5:08PM
Subject: Re: Form SC870

Harley,

Generally we would use an SC870AD at this level and I'm receiving some serious questions about why we should make an exception and execute an SC870.

If I remember correctly, we discussed this back in March or there abouts and you indicated that you needed additional time to review some of the later years computations. Generally we would be expected to have resolved these issues during the 3 months that have passed and the matter has been under review.

I don't have a problem with respect to adding language that will hold the periods open to address the interest computation question. It would however be unusual for us to hold all periods open for other credit or deduction adjustments.

I suggest that we arrange a conference call for Thursday morning. (John Swearingen will be leaving on vacation later on Thursday, so we need to resolve it in the morning if possible to avoid additional delay.) Would 10:30AM EDT work for you? If so, please call or e-mail me and I'll set it up at this end and see if we can get this closed.

7/11/2002 - Harley Priesmeyer, Pat Hobson
John Swearingen + Jan Crangle conference
call. TP wants to avoid all refunds
for income + license. Indicated that
our earlier understanding was they only needed to
review later years. Advised we will agree to 870AD &
sales + use however TP is not prepared to cut a check for
5th. They want until 12/31/02 to complete review. Requested
that they study position & get back with
us.

Thanks.

Jan

>>> "Harley H Priesmeyer" <hhpriesmeyer@duke-energy.com> 07/10/02 12:06PM >>>
Jan - I received your voice mail re why we needed to do a SC870 instead of a SCAD870 form. There are two reasons for it. One, Duke wants to reserve the right to contest the interest computation on the income/license fee and secondly, Duke is planning on filing amended returns for some credits and other deductions/adjustments that were previously not taken for these years.

Hopefully, this will aid you re this matter. I remember seeing some previous correspondence from Burney in which you were ok with Duke signing an 870 form.

If you need anything else on this, please let me know.

****

Harley Priesmeyer
Director, State and Local Taxes
Duke Energy Corporation
P. O. Box 1642
Houston, Texas 77251-1642

Office: 713-989-3285
Fax: 713-989-3280
Cell: 713-501-0725
email: hhpriesmeyer@duke-energy.com

SCDOR00021661

EXHIBIT N

NEXSEN PRUET
JACOBS POLLARD & ROBINSON, LLC
ATTORNEYS AND COUNSELORS AT LAW

Burnet R. Maybank
MEMBER

DIRECT DIAL
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(843) 720-1768
BMaybank@NPJP.COM

March 20, 2002

Mr. John A. Swearingen
Audit Supervisor
Department of Revenue
301 Gervais Street
Columbia, SC 29201

Jan Steensen Crangle, CPA
Manager, Office of Appeals
South Carolina Department of Revenue
Post Office Box 125
Columbia, SC 29214

Re: Selected Duke State and Local Tax Issues.

Dear John and Jan:

The Duke crowd and I met in Charleston (natch) to discuss the settlement proposals contained in your fax of March 18. We have the following counter-proposal.

First, Duke naturally needs to check your figures. (They had not seen your fax prior to the meeting.) I know there have been issues in the past regarding the calculation of interest, but assuming Duke confirms your figures, we offer the following:

SALES TAX

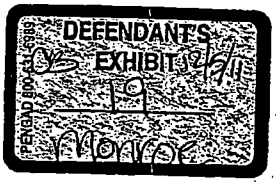
Duke would like to settle the sales tax liability though 2001, using the methodology and quarterly tax liability contained in your fax. (This has the effect of reducing the amount of our refund.) Duke proposes to execute a SC870AD regarding the sales and use tax liability through 2001.

LICENSE TAXES

Subject to verifying the figures, as stated above, Duke proposes accepting the DOR's proposal and executing a SC870AD for license taxes for the years contained in your proposal. (December 1984 to December 1994.)

INCOME TAXES

Subject to verifying the figures, as stated above, Duke proposes accepting the DOR's proposal except that it would agree to execute a SC870, rather than a SC870AD. This would have the effect of keeping the years open for both the DOR and the State until the end of this year, unless the DOR and Duke jointly agree to execute another waiver.



Duke is examining the possibility of filing amended returns for the purposes of claiming tax incentives; as well as possibly other adjustments. In addition, the files are so stale and the number of years open are so large that Duke is reluctant to close out some 16 years without at least some due diligence, which they have not performed.

CONCLUSION

Duke is actively in the process of verifying the figures contained in your fax, which verification is expected to be completed in the next few days. Please let me know what you think about the other points.

Yours very truly,

Burnie

Burnet R. Maybank

BRM/mwj

cc: Mr. Harley Priesmeyer/Duke Energy

EXHIBIT O

ATTACHMENT 1

Code 1976 § 12-7-2210
CODE OF LAWS OF SOUTH CAROLINA 1976 ANNOTATED
TITLE 12. TAXATION
CHAPTER 7. INCOME TAX ACT OF 1926
ARTICLE 19. EXAMINATIONS, DEFICIENCIES AND ILLEGAL OR EXCESSIVE ASSESSMENTS

§ 12-7-2210. Examination of returns; notice and payment of deficiencies; interest and penalties on deficiencies; refunds.

As soon as practicable after each return is filed, the Commission shall examine it and compute the tax and the amount so computed by the Commission shall be the tax. If the tax found due shall be greater than the amount theretofore paid, the excess shall be paid to the Commission within ten days after notice of the amount shall be mailed by the Commission.

If additional tax is found to be due upon the examination of an income tax return and the return has been made in good faith and the understatement of the tax was not due to any fault of the taxpayer there shall be no penalty added because of such understatement, but interest shall be added to the amount of the deficiency at the rate of one half of one per cent for each month or fraction of a month from the date the tax was originally due until the date the deficiency is paid.

If the understatement is due to negligence on the part of the taxpayer, but without intent to defraud, there shall be added to the amount of the deficiency five per cent thereof and in addition interest at the rate of one per cent per month or fraction of a month.

The interest provided for in this section shall in all cases be computed from the date the tax was originally due to the date of payment.

If the amount of tax found due as computed shall be less than the amount theretofore paid, the excess shall be ordered refunded by the Commission.

HISTORY: 1962 Code § 65-321; 1952 Code § 65-321; 1942 Code § 2459; 1932 Code § 2459; 1927 (35) 1, 217; 1959 (51) 144.

HISTORICAL NOTES

EDITOR'S NOTE--

As to provisions of the Internal Revenue Code (26 USCS §§ 1 et seq.) which are specifically not adopted for the purposes of Chapter 7 of Title 12, see the editor's note to § 12-7-10.

REFERENCES

RESEARCH AND PRACTICE REFERENCES--

71 Am Jur 2d, State and Local Taxation § 597.

85 CJS, Taxation §§ 1104(1), 1104(2).

ALR AND L ED ANNOTATIONS--

What is "last known address" of taxpayer for purposes of mailing of notice of tax deficiency under § 6212(b) of the Internal Revenue Code of 1954 (26 USCS § 6212(b)). 58 ALR Fed 548.

ANNOTATIONS

CASE NOTES

Applied in Peoples Nat'l. Bank v South Carolina Tax Comm., 250 SC 187, 156 SE2d 769 (1967).

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ATTACHMENT 2

Code 1976 § 12-7-2220
CODE OF LAWS OF SOUTH CAROLINA 1976 ANNOTATED
TITLE 12. TAXATION
CHAPTER 7. INCOME TAX ACT OF 1926
ARTICLE 19. EXAMINATIONS, DEFICIENCIES AND ILLEGAL OR EXCESSIVE ASSESSMENTS

§ 12-7-2220. Assessment of additional taxes.

If the Commission discovers from the examination of the return or otherwise that the income of the taxpayer or any portion thereof has not been assessed, it may at any time within three years after the time when the return was filed or due to be filed, whichever is later, assess such income and give notice to the taxpayer of such assessment and such taxpayer shall thereupon have an opportunity within thirty days to confer with the Commission as to the proposed assessment. The limitation of three years to the assessment of such tax or additional tax shall not apply in the case of fraud with intent to evade this chapter or authorized rules and regulations promulgated under this chapter or in the case of failure to make a return. After the expiration of thirty days from such notification, the Commission shall assess the income of such taxpayer or any portion thereof which it believes has not heretofore been assessed and shall give notice to the taxpayer so assessed of the amount of the tax and interest and penalties, if any, and the amount thereof shall be due and payable within ten days from the date of such notice. The provisions of this chapter with respect to revision and appeal shall apply to a tax so assessed. No additional tax amounting to less than fifty cents shall be assessed. Provided, that the provisions of this section shall take effect with respect to returns filed or due to be filed after January 1, 1964.

HISTORY: 1962 Code § 65-322; 1952 Code § 65-322; 1942 Code § 2460; 1932 Code § 2460; 1927 (35) 1; 1932 (37) 1311; 1955 (49) 123; 1961 (52) 465; 1967 (55) 495.

HISTORICAL NOTES

EDITOR'S NOTE--

As to provisions of the Internal Revenue Code (26 USCS §§ 1 et seq.) which are specifically not adopted for the purposes of Chapter 7 of Title 12, see the editor's note to § 12-7-10.

REFERENCES

CROSS REFERENCES--

As to provision that the limitation on assessment and collection of taxes in this section is not applicable to collection of deferred taxes on certain receipts from foreign trading, see § 12-7-810.
As to the inapplicability of the time limitations provided in this section to underpayment or overpayment of South Carolina income tax resulting from changes in income made by the Internal Revenue service, see § 12-54-140.

RESEARCH AND PRACTICE REFERENCES--

71 Am Jur 2d, State and Local Taxation § 597.

85 CJS, Taxation §§ 1104(1), 1104(2).

ANNOTATIONS

CASE NOTES

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Where defendant failed to plead limitation of action in state's suit under Code 1962 § 37-132 to recover retaliatory fees from foreign insurance companies, trial court erred by invoking Code 1962 §§ 65-5.1 and 65-322 in limiting state's recovery to 3 of 8 years for which fees were sought. State v Southern Farm Bureau Life Ins. Co. (SC) 219 SE2d 80.

Collection of interest on additional taxes assessed as result of taxpayer's initially accounting under improper method would be inequitable where taxpayer had letter from tax commission requiring it to file return in certain manner and where taxpayer followed these instructions explicitly. Texaco, Inc. v Wasson (1977) 269 SC 255, 237 SE2d 75.

Code § 12-7-2230 is constitutional under Article III, § 17; it is reasonably and inherently related to collection of tax revenues and therefore germane to the General Appropriations Act, and it gives fair notice to the reader that the statute of limitations pertaining to corporate income taxes is being modified. Hercules, Inc. v South Carolina Tax Com. (1980, SC) 262 SE2d 45.

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ATTACHMENT 3

Code 1976 § 12-7-2230
CODE OF LAWS OF SOUTH CAROLINA 1976 ANNOTATED
TITLE 12. TAXATION
CHAPTER 7. INCOME TAX ACT OF 1926
ARTICLE 19. EXAMINATIONS, DEFICIENCIES AND ILLEGAL OR EXCESSIVE ASSESSMENTS

§ 12-7-2230. Corporation shall notify Commission of examination of records by Federal authorities and waiver of limitations as to Federal tax; effect of failure to notify.

Every corporation shall notify the Tax Commission in writing of every examination of its books and records with respect to its net income as reported on its Federal income tax return within thirty days after it has or should have had knowledge of the beginning of such examination by the Internal Revenue Service. When any corporation executes a waiver of the statute of limitations on deficiencies and overassessments of Federal income taxes, it shall notify the Tax Commission in writing within thirty days from the date of such waiver. Failure on the part of the corporation to notify the Tax Commission within the prescribed time of either of the above actions shall automatically suspend the limitations set forth in § 12-7-2220 as amended until ninety days after the Tax Commission receives notice in writing from the corporation of such action.

HISTORY: 1962 Code § 65-322.1; 1971 (57) 709.

HISTORICAL NOTES

EDITOR'S NOTE--

As to provisions of the Internal Revenue Code (26 USCS §§ 1 et seq.) which are specifically not adopted for the purposes of Chapter 7 of Title 12, see the editor's note to § 12-7-10.

ANNOTATIONS

CASE NOTES

This section is constitutional under Article III, § 17; it is reasonably and inherently related to collection of tax revenues and therefore germane to the General Appropriations Act, and it gives fair notice to the reader that the statute of limitations (Code § 12-7-2220) pertaining to corporate income taxes is being modified. Hercules, Inc. v South Carolina Tax Com. (1980, SC) 262 SE2d 45.

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ATTACHMENT 4

Code 1976 § 12-7-2240
CODE OF LAWS OF SOUTH CAROLINA 1976 ANNOTATED
TITLE 12. TAXATION
CHAPTER 7. INCOME TAX ACT OF 1926
ARTICLE 19. EXAMINATIONS, DEFICIENCIES AND ILLEGAL OR EXCESSIVE ASSESSMENTS

§ 12-7-2240. Refund of taxes, penalties, or interest illegally collected; procedure for taxpayer to challenge withholding of refund because of student loan default.

If the commission discovers from the examination of the return or otherwise that the income tax, penalty, or interest paid by any taxpayer is in excess of the amount legally due, the commission may issue its voucher to the Comptroller General for the refund of the illegally collected income tax, penalty, or interest together with the interest provided in Section 12-7-2310. Upon receipt of the voucher, properly executed and endorsed, the Comptroller General shall issue his warrant to the State Treasurer for the payment to the taxpayer of the refund out of any income tax funds in his possession or out of any income tax funds that may come into his possession.

The commission must keep in its files a duplicate of each voucher and also a statement which must set forth the reasons why the refund was ordered.

This section is in addition to any remedies for the abatement or refund of taxes that may otherwise be provided by law.

No refund is allowed or ordered in an amount less than one dollar.

HISTORY: 1962 Code § 65-323; 1952 Code § 65-323; 1942 Code § 2461; 1932 Code § 2461; 1929 (36) 1048; 1960 (51) 1669; 1980 Act No. 423; 1983 Act No. 103 § 1; 1984 Act No. 346; 1985 Act No. 113, § 1; 1985 Act No. 154, Act No 308 § 2; repealed 1988 Act No. 474 § 3, eff October 15, 1988; reenacted and amended 1988 Act No. 668, § 1, eff October 15, 1988.

HISTORICAL NOTES

EDITOR'S NOTE--

As to provisions of the Internal Revenue Code (26 USCS §§ 1 et seq.) which are specifically not adopted for the purposes of Chapter 7 of Title 12, see the editor's note to § 12-7-10.

For provisions providing for the setoff of tax refunds to satisfy delinquent debts owed to state agencies, boards, committees, commissions, public and private institutions of higher learning, and the IRS, see §§ 12-54-410 through 12-54-500.

EFFECT OF AMENDMENTS--

The 1980 amendment added the second sentence to the fourth paragraph.

The 1983 amendment designated the previously undesignated provisions as subsection (A), made technical and grammatical changes therein, and added subsection (B).

The 1984 amendment substantially rewrote subsection (B).

The first 1985 amendment added, to subsection B, that the commission shall notify the Child Support Enforcement Division, upon request, of the home address and social security number of a taxpayer whose name has been submitted to the commission.

The second 1985 amendment added subsection (C).

The 1986 amendment added a new paragraph at the end of subsection (A) relating to the procedure to be followed by a taxpayer challenging the withholding of a refund because of a student loan default.

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The 1988 amendment rewrote this section.

REFERENCES

CROSS REFERENCES--

As to other provisions relating to refund of income tax, see §§ 12-7-2440 and 12-9-380.
As to the prohibition against any agent or employee of the state tax commission or the state auditor's office disclosing any records of and reports and returns filed with the commission, see § 12-54-240.
As to collection of employment security benefits overpayments, see § 41-41-40.
As to obtaining support payments from absent parents, see § 43-5-220.

HISTORICAL NOTES

FEDERAL ASPECTS--

As to collection of past-due support from federal tax refunds, see 42 USCS § 664.

REFERENCES

RESEARCH AND PRACTICE REFERENCES--

71 Am Jur 2d, State and Local Taxation §§ 608 et seq.

ANNOTATIONS

CASE NOTES

This section [Code 1962 § 65-323] does not create a plain ministerial duty on the part of the Tax Commission to refund any and all overpaid income taxes assessed and collected against taxpayers prior to the passage of this law, without regard to the legality or equity of such claims. Argent Lbr. Co. v Query, 178 SC 1, 182 SE 93 (1935).

The Tax Commission's authority to order a refund is limited by the terms of this section [Code 1962 § 65-323] in its scope, and it confers the power and authority upon the Tax Commission to refund illegally collected income tax, penalty or interest, when it discovers from the examination of the return or otherwise that the amount paid by any taxpayer is in excess of the amount legally due; this allowance of such a refund is not made obligatory, and no provision for its enforcement by the taxpayer by suit against the State, without its consent, is contained in this section [Code 1962 § 65-323]. Argent Lbr. Co. v Query, 178 SC 1, 182 SE 93 (1935).

Section does not authorize taxpayer's suit for refund.--Under the terms of this section [Code 1962 § 65-323] the Tax Commission is clothed with the power and authority to make such refunds for valid reasons, but no corresponding right is conferred upon the taxpayer to compel by suit the exercise of this authority. Argent Lbr. Co. v Query, 178 SC 1, 182 SE 93 (1935).

State must consent to suit against Commission.--A suit by a taxpayer against the Tax Commission for the recovery of interest on refunded taxes, is a suit against the State, and may not be instituted without the consent of the State. Monarch Mills v South Carolina Tax Comm., 149 SC 219, 146 SE 870 (1929).

For additional related case, see Southern Ry. Co. v Query, 21 F2d 333 (1927).

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EXHIBIT P

hereunder shall be considered to be of the par value of ($100.00) per share. Said fees shall be due and payable as hereinbefore provided each and every year to the Secretary of State, who shall pay the same into the State Treasury. Upon failure to file the papers and information as herein required at the times provided then shall be added a penalty of the sum of Ten Dollars per day each and every day the same is in default and if unpaid for sixty days after the same is due and payable, the corporation in default shall be prohibited from doing business in this State until the amounts due with the penalties are paid. The fees herein provided authorize the corporation to transact its business during the year, or for any fractional part of such year, in which such fees are paid.

§ 2. This Act shall take effect immediately upon its approval by the Governor.

§ 3. All Acts or parts of Acts inconsistent with this Act are hereby repealed.

Approved the 20th day of March, 1923.

No. 11.

AN ACT to Raise Revenue for the Support of the State Government.

Section 1. Taxes Levied.—Be it enacted by the General Assembly of the State of South Carolina: That on and after April 1, 1923, there shall be levied, collected, and paid, for and in respect of the several bonds, debentures, or certificates of stock and of indebtedness, and other documents, instruments, matters, and things mentioned and described in Schedule A of this Act, or for or in respect of the vellum, parchment, or paper upon which such instruments, matters, or things, or any of them, are written or printed, by any person who makes, signs, issues, sells, removes, consigns, or ships the same, or for whose use or benefit the same are made, signed, issued, sold, removed, consigned, or shipped, the several taxes specified in such schedule.

§ 2. Exemptions, Governmental and Municipal Securities, etc.—Certain Mutual Companies.—That there shall not be taxed

under this Act any bond, note, or other instrument, issued by the United States, or by any foreign Government, or by any State, Territory, or the District of Columbia, or local subdivision thereof, or municipal or other corporation exercising the taxing power: or any bond of indemnity required to be filed by any person to secure payment of any pension, allowance, allotment, relief, or insurance by the United States, or to secure a duplicate for, or the payment of, any bond, note, certificate of indebtedness, war-savings certificate, warrant or check, issued by the United States. Or stocks and bonds issued by cooperative building and loan associations which are organized and operated exclusively for the benefit of their members and make loans only to their shareholders, or by mutual ditch or irrigation companies.

§ 3. Penalties for Evasions of Stamp Tax—Compromise of Prosecutions.—That whoever—

(a) Makes, signs, issues, or accepts, or causes to be made, signed, issued, or accepted, any instrument, document, or paper of any kind, or description whatsoever without the full amount of tax thereon being duly paid;

(b) Makes use of any adhesive stamp to denote any tax imposed by this Act, without cancelling or obliterating such stamp as prescribed in Section 5;

Is guilty of a misdemeanor and upon conviction thereof shall pay a fine of not more than One Hundred ($100.00) Dollars for each offense: *Provided,* The South Carolina Tax Commission may compromise any civil or criminal case arising under the provisions of this Act instead of commencing suit thereon, and may compromise any such case with the consent of the Attorney General after suit thereon has been commenced. Where any case is compromised the South Carolina Tax Commission shall keep on file in the office of the State Tax Commission reasons for settlement of any case by compromise, together with a statement of the amount of tax assessed, the amount of additional tax or penalty or interest imposed by law in consequence of the neglect or delinquency of the person against whom the tax is assessed, and the amount actually paid in accordance with the terms of the compromise.

§ 4. Fraud in use of Stamps—Possession of Stamps for Re-use—Penalty.—That whoever—

son, firm or corporation doing business within the State of South Carolina and engaging in the business of selling at retail or in any individual instance selling to the final consumer, such articles as are named in this Section, for the privilege of carrying on such business, shall be subject to the payment of a license tax which shall be measured by and graduated in accordance with the volume of sales of such person, firm or corporation, as follows:

(a) There shall be levied, assessed, collected and paid upon all ammunition, including shells for shotguns and cartridges for rifles, pistols, revolvers, automatic pistols, rifles and machine guns, and upon such shells and cartridges partially prepared for use but lacking powder or shot or other necessary constituent, and upon blank shells and cartridges (but not upon powder or shot or caps not prepared and not in form to use in modern firearms), when sold at retail or to the ultimate consumer, the following:

Upon all shotgun or other shells, two ($2.00) dollars per thousand rounds;

Upon all cartridges, twenty-five (25) calibre or greater, two ($2.00) dollars per thousand rounds.

(b) The license taxes imposed upon ammunition shall be paid by stamps to be affixed and cancelled by the retailer or other final seller, and said stamps shall be affixed to the smallest container in which or from which the articles are sold, as soon as the original packages are opened or broken, or if received in no other form than that in which sold, as soon as the containers are placed in the place of business of the retailer; in the case of articles intended for sale in the packages in which received from outside the State of South Carolina without opening or alteration of any sort, each package must be immediately marked with the date of receipt and the place from which received and no stamps need be affixed so long as such package remains unopened and unaltered.

(c) There shall be levied, assessed, collected and paid upon all candy when sold at retail or to the ultimate consumer, the following:

Upon all candy retailing at eighty cents per pound and above ten (10) per centum.

(d) The license taxes imposed upon candy shall be collected by the final seller and paid to the South Carolina Tax Commission in accordance with such rules and regulations as may be issued

by the South Carolina Tax Commission, said rules and regulations to have full force and effect of law.

(e) There shall be levied, assessed, collected and paid upon all admissions to places of amusement within the State of South Carolina, a license tax of one ($0.01) cent for each ten ($0.10) cents or fractional part thereof: *Provided,* That admissions to theatres located in incorporated towns of less than two thousand population shall be exempt from the provisions of this Act: *Provided, further,* That admissions to any place of amusement where the proceeds or benefits inure directly to religious, charitable, educational, eleemosynary organizations, or to any agricultural or industrial society, community or associations, shall be exempt from the provisions of this Act; nor shall the provisions of this Act apply to any collegiate or public school amusement; nor to any swimming pool where picnic grounds are maintained free.

(f) The license tax imposed upon admissions to places of amusement shall be paid in accordance with such rules and regulations as may be issued by the South Carolina Tax Commission, said rules and regulations to have the full force and effect of law.

§ 11-A. License Tax on Manufacturing—on Mining.—That every person, firm or corporation engaged in the business of manufacturing or mining shall be subject to the payment of a license tax of one-tenth of one per cent., which shall be measured by and graduated in accordance with:

(a) In the case of manufacturing the entire receipts, including all sums earned or charged, whether actually received or not, and in the case of any article manufactured in whole or in part within this State, and not sold or disposed of in this State, the value thereof shall be included.

(b) In the case of mining, the value of the products of such mines, including all sums earned or charged, whether actually received or not, in connection with the said mining business.

§ 11-B. Reports—Assessment of Tax—Powers of Tax Commission—Appeals—Penalties.—It shall be the duty of the individual or the superintendent or other officer in charge of any mine, factory or other manufacturing establishment now engaged, or which may hereafter be engaged, in operation, to assess the license hereby imposed from time to time as the raw material is

mined or manufactured and is ready for shipment or market, and to ascertain and assess the actual value of the articles mined or manufactured, and to fix the value thereof; the said individual, superintendent or other officer in charge of any such mine, factory or manufacturing plant in operation, or that shall hereafter come into operation, shall annually, on or before the first day of January of the calendar year next preceding, file a report in writing, under oath, to the State Tax Commission on the forms furnished and prescribed by it, stating specifically the amount of such finished products subject to license and the assessed valuation thereof during the calendar year covered by the report, and the amount due thereon: *Provided,* That the report made on or before the first day of January, 1924, shall be for the portion of the year 1923 remaining after this Act becomes effective and in operation.

If the State Tax Commission is not satisfied with the assessment and estimate of valuation so made and returned, as aforesaid, they are hereby authorized and empowered to make an assessment of valuation based upon the facts contained in the report herein required, or upon any information within their possession, or that shall come into their possession, and to settle and account for the assessment of valuation so made by them and the taxes, penalties and interest due the State of South Carolina therein, with the right to the person, corporation, company, owner or operator dissatisfied with any settlement so made against him, it, or them, to appeal therefrom in the manner now provided by law for appeals from the decision of the State Tax Commission to the State Board of Tax Reviewers. For the purpose of making such assessment and settlement, said officers may require the production of such books, papers, reports, etc., as may be necessary to enable them to assess and settle the tax.

In the event of the failure, neglect or refusal of the individual, superintendent or other officer in charge of any mine, factory or manufacturing plant to make the report and valuation to the State Tax Commission, as hereinbefore provided, on or before the first day of January of each and every year, it shall be the duty of the State Tax Commission to estimate an assessment of valuation of the products in such mine, factory or manufacturing company which have been prepared for market by any person, firm, corporation, owner or operator, as aforesaid, and settle and account for the taxes, penalties and interest thereon, from which settlement there shall

be no right of appeal; and the penalty shall be that now fixed by law for the non-payment of taxes, and the interest shall be at a rate not exceeding five (5) per centum.

Any person, firm, corporation, owner, operator or lessee of any mine, factory or manufacturing establishment from which a report is required under the provisions of this Act, shall pay into the Treasury of the State of South Carolina the amount of the license herein imposed within sixty (60) days from the date of the settlement of the account by the State Tax Commission, plus a penalty of one (1) per centum for their failure to assess said license and to make a report as required by this Act. When any license is settled, it shall bear interest from sixty (60) days after approval by the State Tax Commission, at the rate of five (5) per centum per annum, until paid.

If any individual, superintendent or other officer of any firm, corporation, limited partnership or joint stock association, or any lessee of any mine, factory or other manufacturing company, shall neglect or refuse to furnish the State Tax Commission, on or before the first day of January of each and every year, with the assessments and report as aforesaid, as required by law, or cause the same to be done, or make or cause to be made any false report, it shall be the duty of the State Tax Commission to add ten (10) per centum to said tax for each and every year for such assessment and report not so furnished, which per centum shall be settled and collected with the said tax in the usual manner of settling accounts and collecting such tax. The State Tax Commission may, upon application made before the first day of January of each and every year, and upon proper cause shown, extend the time of filing returns for a period not exceeding fifteen (15) days from the first day of January of the year in which the same are required to be filed.

If the said persons or officers, or any of them, shall intentionally make, or cause to be made, any false assessment or report, or intentionally neglect or refuse to furnish the State Tax Commission with the assessment and report as required by law, he or they shall be guilty of a misdemeanor, and upon conviction thereof shall be sentenced to pay a fine of five hundred ($500.00) dollars and undergo imprisonment for not exceeding one year, or both, or either, at the discretion of the Court.

That this Act shall be administered by the State Tax Commission and all monies derived herefrom shall be turned over to the State Treasurer and used for the purpose of running the State Government: *Provided*, That the State Tax Commission is hereby authorized and empowered to promulgate such rules and regulations as it may deem expedient and proper to carry out the provisions of this Act.

§ 11-C. Provisions of Act Independent.—The provisions of this Act shall be independent of each other, and if any of its provisions shall be held to be unconstitutional, the decision of the Court shall not affect or impair any of the remaining provisions of this Act, nor prevent the collection of the tax imposed by this Act. It is hereby declared the legislative intent that this Act would have been adopted had such unconstitutional provision not been included therein.

§ 12. Floor Tax Upon Articles on Hand when Act Takes Effect.—That upon all articles enumerated in this Act which are, on the day after the date this Act shall go into effect, held by any person, firm or corporation and intended for sale, there shall be levied, assessed, collected and paid a floor tax equal to the tax imposed by this Act upon such articles or commodities.

§ 13. Regulations for Enforcement—Penalty for Violation—Affixing of Stamps—Penalties for Fraud and Misuse of Stamps.—(a) It shall be provided by regulations of the Tax Commission that methods of breaking packages, forms and kinds of containers, and methods of affixing stamps, shall be employed by individuals and companies subject to the tax imposed by this Act which will make possible enforcement of payment by inspection; and any individual or company subject to this tax, engaging in or permitting such practices as are prohibited by regulations of the Tax Commission, or in any other practice which make it difficult to enforce the provisions of this Act by inspection shall be deemed to be guilty of a misdemeanor and shall, upon conviction, be fined not less than one hundred ($100.00) dollars for each offense, or imprisonment for a period not exceeding thirty (30) days, or both, in the discretion of the Court.

(b) Stamps shall be affixed in such manner that their removal will require continued application of steam or water and they shall be cancelled when affixed, the cancellation consisting of any disfigu-

ration which cannot be erased without the use of chemicals or scraping.

(c) Persons failing to affix properly stamps, or to cancel after affixed, shall be subject to the provisions of Section 7 of this Act, and for each offense shall pay as a part of the tax imposed by this Act, a penalty of twenty ($20.00) dollars for the first offense; fifty ($50.00) dollars for the second offense, and one hundred ($100.00) dollars for each offense thereafter: *Provided*, That the South Carolina Tax Commission may compromise any civil case arising under the provisions of this Act instead of commencing suit thereon, and may compromise any criminal case with the consent of the Attorney General before or after prosecution thereon has been commenced. When any case is compromised, the South Carolina Tax Commission shall keep on file in the office of said Commission reason for settlement of any case by compromise, together with a statement of the amount of tax assessed, the amount of additional tax or penalty or interest imposed by law in consequence of the neglect or delinquency of the person, firm or corporation against whom the tax is assessed, and the amount actually paid in accordance with the terms of the compromise.

(d) That whoever willfully removes or alters the cancellation or defacing marks of, or otherwise prepares any adhesive stamp, with intent to use, or cause the same to be used, after it has already been used, or knowingly or willfully buys, sells, offers for sale, or gives away, any such washed or restored stamp, to any person for use, or knowingly uses the same, or has in possession any washed, restored or altered stamp, which has been removed from the article to which it had been previously affixed, is guilty of a misdemeanor, and, upon conviction thereof, shall be punished by a fine of not more than one thousand ($1,000.00) dollars, or by imprisonment for not more than five (5) years, or both, in the discretion of the Court.

§ 14. Tax Commission to Enforce Act—Entry on Premises—Inspection of Documents.—The South Carolina Tax Commission shall administer and enforce the taxes imposed by this Act. It shall have power to enter upon the premises of any taxpayer and to examine, or cause to be examined, by any agent or representative, designated by it for that purpose, any books, papers, records, or memoranda, bearing upon the amount of taxes payable, and to secure other information directly concerned in the enforcement of this Act.

Act, and all such remittances shall be accompanied with a typewritten statement showing the sources from which the said license tax or taxes were derived. That the South Carolina Tax Commission shall furnish the Comptroller General with a true copy of all remittance sheets which said Commission is required by this Act to send to the State Treasurer.

§ **25. Exemptions from Section 3.**—That every person, firm or corporation taxable under the provisions of Sections one (1) and two (2) of this Act shall not be subject to any tax imposed by Section three (3) of this Act.

§ **26. Substitutes for Stamps.**—That in case of failure for any cause to provide the necessary stamps required by this Act the Tax Commission is hereby empowered to make and promulgate such temporary substitute as it may deem expedient until such stamps can be procured and offered for sale.

§ **27.** All Acts or parts of Acts inconsistent with the provisions of this Act are hereby repealed.

§ **28.** This Act shall take effect May 1st, 1923.

Approved the 26th day of March, A. D. 1923.

No. 12.

AN ACT to Make it Unlawful for Any Person to Impersonate or Attempt to Impersonate Another Person for the Purpose of Voting in Any Party Primary Election, or Special or General Election, Both Municipal and State, Providing for a Penalty for Same and Notice to Be Given in Cities of Forty Thousand Inhabitants and More, and to Provide for the Forfeiture of Bond, Etc.

Section 1. Impersonation of Voter Unlawful—Arrest.—Be it enacted by the General Assembly of the State of South Carolina: On and after the approval of this Act by the Governor it shall be unlawful for any person to impersonate or attempt to impersonate another person for the purpose of voting in any primary election of this State, whether municipal or State, and any general and special election, whether municipal or State: *Provided,* That

EXHIBIT Q

No. 468.

A JOINT RESOLUTION to Exempt Certain Manufactories in York, Richland, Lancaster, Georgetown, Greenwood, Marion, Sumter, Clarendon, Cherokee, Saluda, and Laurens Counties From County Taxes for a Period of Five Years.

Section 1. Tax Exemption of Manufactories in Certain Counties.—Be it resolved by the General Assembly of the State of South Carolina: Any and all manufactories desiring to locate in the Counties of York, Richland, Lancaster, Georgetown, Greenwood, Marion, Sumter, Clarendon, Cherokee, Saluda and Laurens, with a capital of not less than one hundred thousand ($100,000.00) dollars shall be exempt from all county taxes, except for school purposes, for five (5) years from the time of their establishment.

§ 2. All Acts or parts of Acts inconsistent herewith are hereby repealed.

§ 3. This Resolution shall take effect immediately upon its approval by the Governor.

Approved the 5th day of March, A. D. 1925.

No. 469.

AN ACT to Abolish the Office of Public Cotton Weigher in the Town of York, York County.

Section 1. Office of Cotton Weigher at York Abolished —Proviso.—Be it enacted by the General Assembly of the State of South Carolina: That the office of Public Cotton Weigher for the town of York, York County, is hereby abolished and there shall be no Public Cotton Weigher in said town of York: *Provided, however,* That the office of Public Cotton Weigher at York may be reinstituted at any future time, in the manner as now provided by law.

§ 2. All Acts or parts of Acts inconsistent with this Act are hereby repealed.

§ 3. This Act shall take effect immediately upon its approval by the Governor.

Approved the 14th day of March, A. D. 1925.

EXHIBIT R

STATE OF SOUTH CAROLINA
ADMINISTRATIVE LAW COURT

Duke Energy Corporation, Petitioner, vs. South Carolina Department of Revenue, Respondent,	)	Docket No. 10-ALJ-17-0270-CC

Affidavit of Glenn J. Robinson, M.S., P.E.

1. I am over eighteen (18) years of age and of sound mind and qualified to give this affidavit.

2. I have a B.S. and M.S. in Electrical Engineering from the University of Washington.

3. I presently am a consulting electrical engineer with Engineering Design & Testing Corp. located in Columbia, South Carolina.

4. I have worked as an electrical engineer for more than 48 years.

5. My curriculum vita is attached as Exhibit A.

6. I have been retained by the South Carolina Department of Revenue to provide an opinion regarding the nature of electricity, electrical generation, and electricity in commerce.

7. In my opinion, generating electricity constitutes manufacturing.

8. The process of generating electricity by electric utilities such as Duke Energy requires the use of large generators and other capital-intensive equipment.

9. The delivery of electricity to consumers requires the use of a large and capital-intensive system of wires, poles, transformers, and other equipment for delivery of the electricity to the consumer through a transmission and distribution network.

10. When electric utilities such as Duke Energy operate generators, they generate electricity for use by consumers.

11. The electricity that is generated by electric utilities such as Duke Energy would not be available for use by consumers in the absence of the generation and distribution system in which the utilities have invested significant amounts of capital.

12. In my opinion, electricity is tangible personal property.

13. In my opinion, electricity is a good and a commodity.

14. Electricity can be sensed by a person or a consumer, such as by a child placing their finger into an electrical outlet on the wall of a home.

15. From a consumer's standpoint, electricity is seen through the instance of an arc light.

16. Similarly, electricity can, from a consumer's standpoint, be touched and felt through exposure to electrical current.

17. Electricity can be stored in a battery and drawn from that battery at a later time.

18. The flow of electricity can be measured by use of a meter like that found on the side of most people's homes.

19. Electricity is movable and is moved by companies such as Duke Energy and delivered to consumers through a network of transmission and distribution lines and systems.

20. Electricity may be identified as evidenced by the measurement that takes place when it passes through a meter and is delivered to the consumer for use.

21. In sum, electricity has unique physical characteristics.

22. Electricity is a tangible means of conveying electrical energy for powering machinery and equipment and household appliances.

23. In the absence of the unique characteristics of electricity, consumers could not operate their machinery and equipment or household appliances.

[SIGNATURE AND NOTARIZTION PAGE FOLLOWS]

This 1 day of June, 2012.

Glenn Robinson

Sworn to and subscribed before me,
this 1st day of June 2012

Notary Public for the State of South Carolina
My Commission expires: 2/11/2018

EXHIBIT A

ENGINEER: ELECTRICAL

GLENN J. ROBINSON, M.S., P.E.
Engineering Design & Testing Corp.
Post Office Box 8027
Columbia, South Carolina 29202

EDUCATION:

1963 B.S. Electrical Engineering - University of Washington
1968 M.S. Electrical Engineering - University of Washington

PROFESSIONAL EXPERIENCE:

August, 1999 to present **Engineering Design & Testing Corp. - Columbia, South Carolina**
Consulting Electrical Engineer responsible for consultation with insurance companies, manufacturing industries, government and attorneys. Specific areas of expertise include: Evaluation of distribution and plant-wide electrical systems; review and evaluation of instrumentation and process control systems; troubleshooting and failure analysis of electric and control networks; evaluate cause of damage, scope of damage and cost of repair of electrical systems and equipment.

1995 to 1999 **Fibermark, Inc. - Warren & Hughesville Mills, New Jersey**
Electrical Superintendent responsible for electrical and instrument (E&I) engineering and boiler/generator administration. Implement modern controls for secondary fiber system and stock refiner. Major rebuild and startup of Hughesville dry end including complete rewiring and drive modifications in conjunction with equipment upgrade.

1992 to 1995 **Getchell Gold, Inc., Getchell Mine - Golconda, Nevada**
Project Engineer responsible for capital projects tracking and budgeting, project and E&I engineering, piping, E&I and facility design and major overhaul of demineralizer, boiler and deaerator piping and controls. Add 15 MVA electrical substation and 13KV mine feeder line (specification, procurement, design, installation and startup). Commission and start up underground mine distribution substation.

1991 to 1992 **Pitt County Memorial Hospital - Greenville, North Carolina**
Electrical Engineer responsible for project and electrical engineering. Specific projects included LAN repeater room and network extension installation, CT room layout (foundation, structure and electrical design) and miscellaneous electrical and lighting changes.

1986 to 1991	**Weyerhaeuser Company, Lumber Facility - Ayden, North Carolina** Engineering Manager responsible for scope, design, permitting and procurement of $60 million green-field sawmill. Responsible for plant, processing and system engineering during and after construction, electric, water and sewer utility coordination and participation in process and process control startup. Leadership and hands-on participation in numerous process improvement projects. Develop production planning software and validated and improved log sorting control software.
1979 to 1985	**Weyerhaeuser Company Wood Products R&E - Tacoma, Washington** Project Manager responsible for a manufacturing control system development program, related projects and transverse bucking system from concept through start-up and acceptance (first of several implementations). Stem scanner development and field test, benefit tests, system requirements, cost estimate, capital approval, team building, cost control, key software validation, startup tuning and acceptance.
1974 to 1978	**The Oregon Graduate Institute - Beaverton, Oregon** Staff Engineer responsible for instrument development, implementation and technical supervision. Instrumentation developed included lighting strike monitor for Bonneville Power HV transmission lines, a non-contacting lumber thickness gauge, a control product introduction for an electronics distributor and numerous monitor and data systems for researchers. Managed instrument maintenance and computer center.
1965 to 1974	**The University of Washington - Seattle, Washington** Staff Engineer responsible for instrument development, implementation and technical supervision.
1963 to 1965	**The Boeing Company - Seattle, Washington** Staff Engineer responsible for parts of missile and radar system proposals.

REGISTRATIONS:

Registered Professional Engineer in South Carolina (#20297)
Registered Professional Engineer in North Carolina (#017548)
Registered Professional Engineer in Washington (#11097)
Registered Professional Engineer in Georgia (#028024)
Registered Professional Engineer in Ohio (#72945)
Registered Professional Engineer in Indiana (# 10809491)
National Council for Engineering and Surveying (#22912)

EXHIBIT S

STATE OF SOUTH CAROLINA

ADMINISTRATIVE LAW COURT

DUKE ENERGY CORPORATION,

Petitioner(s),

vs. Case No: 10-ALJ-17-0270-CC

SOUTH CAROLINA DEPARTMENT OF REVENUE,

Respondent(s).

D E P O S I T I O N

WITNESS: GLENN J. ROBINSON, M.S., P.E.

DATE: Wednesday, January 4, 2012

TIME: 10:31 a.m.

LOCATION: Willoughby & Hoefer, P.A.
930 Richland Street
Columbia, South Carolina

TAKEN BY: Attorneys for the Petitioner

REPORTED BY: SHERI L. BYERS
Registered Professional Reporter

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BY MR. TRESH:

Q. You mentioned a moment ago the fact that you could meter -- we were talking about the idea that the service of transmitting from Duke's facility to the customer's home, the important thing, while you believe that's a material, is that it can be metered, right? You testified to that?

A. Yes.

Q. Can you meter cell phone minutes?

A. Absolutely. You can meter attorney hours. You can meter engineering hours.

Q. Does that make any of these things material?

A. No, it does not. That is an exception based on the idea that if I charge my client for doing the same work twice, I am cheating my client. It's not commoditized.

Q. In the cell phone example, which we said can be metered --

A. Yes.

Q. -- the cell phone call would then be a material in your definition; is that correct?

A. No. A cell phone call is not a material in my definition. It's a time-based service.

Q. Hang on. I believe you testified a moment ago that cell phone calls can be metered; is that

correct?

A. Yes.

Q. Okay. So they can be metered. And you also testified that if something can be metered, it's a material?

A. No.

Q. That's not true?

A. Because right in front of you, I would conclude that a product, other than hours of service, can be metered, it is the result of manufacturing, not service. So if you want to go into hours of service, then, no, it's not manufactured. But if you're paying by quantity of goods transferred, then it is manufactured.

Q. So if I could buy cell phone service in some other way than hours of service, which I can.

A. Yes. You can do a flat rate.

Q. Right.

A. So could Duke. Duke could charge me $30 a month, and I could use as little or as much as I want. That would be a service. That would be definitely a service.

Q. Okay. So in your view, electricity -- the electricity that Duke sells, the electric energy that Duke sells, it would change from a material to a